
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934

For the Fiscal Year Ended December 31, 2013

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Transition Period from _____ to _____

Commission File Number 1-5581



WATSCO, INC.

(Exact name of registrant as specified in its charter)

FLORIDA
(State or other jurisdiction of
incorporation or organization)

59-0778222
(I.R.S. Employer
Identification No.)

**2665 South Bayshore Drive, Suite 901
Miami, FL 33133**
(Address of principal executive offices, including zip code)

(305) 714-4100
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common stock, \$0.50 par value	New York Stock Exchange and the Professional Segment of NYSE Euronext in Paris
Class B common stock, \$0.50 par value	New York Stock Exchange

Securities registered pursuant to section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities and Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES NO

The aggregate market value of the registrant's voting common equity held by non-affiliates of the registrant as of June 28, 2013, the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$2,159 million, based on the closing sale price of the registrant's common stock on that date. For purposes of determining this number, all named executive officers and directors of the registrant as of June 28, 2013 were considered affiliates of the registrant. This number is provided only for the purposes of this Annual Report on Form 10-K and does not represent an admission by either the registrant or any such person as to the affiliate status of such person.

The registrant's common stock outstanding as of February 21, 2014 comprised (i) 30,046,979 shares of Common stock, excluding 6,322,650 treasury shares, and (ii) 4,762,288 shares of Class B common stock, excluding 48,263 treasury shares.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Parts I and II is incorporated by reference from the registrant's 2013 Annual Report, attached hereto as Exhibit 13. The information required by Part III (Items 10, 11, 12, 13 and 14) is incorporated herein by reference from the registrant's definitive proxy statement for the 2014 annual meeting of shareholders (to be filed pursuant to Regulation 14A).

WATSCO, INC. AND SUBSIDIARIES

Form 10-K
For the Fiscal Year Ended December 31, 2013

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PART I

Forward-Looking Statements

This Annual Report on Form 10-K contains or incorporates by reference statements that are not historical in nature and that are intended to be, and are hereby identified as, “forward-looking statements” as defined in the Private Securities Litigation Reform Act of 1995, including statements regarding, among others, (i) economic conditions, (ii) business and acquisition strategies, (iii) potential acquisitions and/or joint ventures, (iv) financing plans and (v) industry, demographic and other trends affecting our financial condition or results of operations. These forward-looking statements are based on management’s current expectations and are subject to a number of risks, uncertainties and changes in circumstances, certain of which are beyond their control.

Actual results could differ materially from these forward-looking statements as a result of several factors, including, but not limited to:

- *general economic conditions;*
- *competitive factors within the HVAC/R industry;*
- *effects of supplier concentration;*
- *fluctuations in certain commodity costs;*
- *consumer spending;*
- *consumer debt levels;*
- *new housing starts and completions;*
- *capital spending in the commercial construction market;*
- *access to liquidity needed for operations;*
- *seasonal nature of product sales;*
- *weather conditions;*
- *insurance coverage risks;*
- *federal, state and local regulations impacting our industry and products;*
- *prevailing interest rates;*
- *foreign currency exchange rate fluctuations;*
- *international political risk; and*
- *the continued viability of our business strategy.*

In light of these uncertainties, there can be no assurance that the forward-looking information contained herein will be realized or, even if realized, in whole or in part, that the information will have the expected consequences to, or effects on, our business or operations. For additional information regarding other important factors that may affect our operations and could cause actual results to vary materially from those anticipated in the forward-looking statements, see our SEC filings, including but not limited to, the discussion included in Item 1A “Risk Factors” of this Annual Report on Form 10-K. Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information or the discussion of such risks and uncertainties to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information, except as required by applicable law.

ITEM 1. BUSINESS

General

Watsco, Inc. and its subsidiaries (collectively, “Watsco,” or *we, us or our*) was incorporated in Florida in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies (“HVAC/R”) in the HVAC/R distribution industry in North America. At December 31, 2013 we operated from 569 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean, through which we serve more than 50,000 contractors and dealers that service the replacement and new construction markets. Our revenues in HVAC/R distribution have increased from \$64.1 million in 1989 to \$3.7 billion in 2013, resulting from our strategic acquisition of companies with established market positions and subsequent building of revenues and profit through a combination of additional locations, products, services and other initiatives.

Our principal executive office is located at 2665 South Bayshore Drive, Suite 901, Miami, Florida 33133, and our telephone number is (305) 714-4100. Our website address on the Internet is www.watsco.com and e-mails may be sent to info@watsco.com. The reference to our website address does not constitute incorporation by reference of the information contained on, or linked to, the website, and none of such information is part of this report.

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Residential Central Air Conditioning, Heating and Refrigeration Industry

The HVAC/R distribution industry is highly fragmented with approximately 2,300 distribution companies. The industry in the United States and Canada is well-established, having had its primary period of growth during the post-World War II era with the advent of affordable central air conditioning and heating systems for both residential and commercial applications. The advent of HVAC/R products in Latin America and the Caribbean is also well-established, but has emerged in more recent years as those economies have grown and products have become more affordable and have matured from luxury to necessity.

Based on data published in the IBISWorld Industry Report for Heating and Air Conditioning Wholesaling in the U.S. and other available data, we estimate that the annual market for residential central air conditioning, heating and refrigeration equipment and related parts and supplies in the Americas is approximately \$35.0 billion. Residential central air conditioners are manufactured primarily by seven major companies that together account for approximately 90% of all units shipped in the United States each year. These companies are: Carrier Corporation (“Carrier”), a subsidiary of United Technologies Corporation; Goodman Manufacturing Company, L.P. (“Goodman”), a subsidiary of Daikin Industries, Ltd.; Rheem Manufacturing Company (“Rheem”); Trane Inc., a subsidiary of Ingersoll-Rand Company Limited; York International Corporation, a subsidiary of Johnson Controls, Inc.; Lennox International, Inc.; and Nordyne Corporation (“Nordyne”), a subsidiary of Nortek Corporation. These manufacturers distribute their products through a combination of factory-owned and independent distributors who, in turn, supply the equipment and related parts and supplies to contractors and dealers nationwide that sell to and install the products for consumers, businesses and other end-users.

Air conditioning and heating equipment is sold to the residential replacement market, the commercial market and residential new construction market. The replacement market has increased in importance over the past several years as a result of the aging of the installed base of residential central air conditioners and furnaces, the introduction of new higher energy efficient models, the remodeling and expansion of existing homes, the addition of central air conditioning to homes that previously had only heating products and consumers’ overall unwillingness to live without air conditioning or heating products. The mechanical life of central air conditioning and furnaces varies by geographical region due to usage and ranges from approximately 8 to 20 years. According to data published by the Energy Information Administration, there are approximately 89 million central air conditioning and heating systems installed in the United States that have been in service for more than 10 years. Many installed units are currently reaching the end of their useful lives, which we believe will provide a growing and stable replacement market.

We also sell products to the refrigeration market. These products include condensing units, compressors, evaporators, valves, refrigerant, walk-in coolers and ice machines for industrial and commercial applications. We distribute products manufactured by Copeland Compressor Corporation, a subsidiary of Emerson Electric Co. (“Emerson”), E. I. Du Pont De Nemours and Company (“DuPont”), Mueller Industries, Inc., Owens Corning Insulating Systems, LLC and The Manitowoc Company, Inc. (“Manitowoc”).

Business Strategy

We have a “buy and build” strategy that has produced substantial long-term growth in revenues and profits. The “buy” component of the strategy focuses on acquiring market leaders to either expand into new geographic areas or gain additional market share in existing markets. We employ a disciplined and conservative approach that seeks opportunities that fit well-defined financial and strategic criteria. The “build” component of the strategy focuses on implementing a growth culture at acquired companies, by adding products and locations to better serve customers, exchanging ideas and business concepts amongst the executive management teams and investing in new technologies. Newly acquired businesses have access to our capital resources and established vendor relationships to provide their customers with an expanded array of product lines on favorable terms and conditions with an intensified commitment to service.

Strategy in Existing Markets

Our strategy for growth in existing markets focuses on customer service and product expansion to satisfy the needs of the higher growth, higher margin replacement market, in which customers generally demand immediate, convenient and reliable service. We respond to this need by (i) offering a broad range of product lines, including the necessary equipment, parts and supplies to enable a contractor to install or repair a central air conditioner, furnace or refrigeration system, (ii) maintaining a strong density of warehouse locations for increased customer convenience, (iii) maintaining well-stocked inventories to ensure that customer orders are filled in a timely manner, (iv) providing a high degree of technical expertise at the point of sale and (v) developing and implementing technology to further enhance customer service capabilities. We believe these concepts provide a competitive advantage over smaller, less-capitalized competitors that are unable to commit resources to open and maintain additional locations, implement technological business solutions, provide the same range of products,

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maintain the same inventory levels or attract the wide range of expertise that is required to support a diverse product offering. In some geographic areas, we believe we have a competitive advantage over factory-operated distributor networks, which typically do not maintain inventories of parts and supplies that are as diversified as ours and which have fewer warehouse locations than we do, making it more difficult for these competitors to meet the time-sensitive demands of the replacement market.

In addition to the replacement market, we sell to the new construction market, including new homes and commercial construction. We believe our reputation for reliable, high-quality service and relationships with contractors, who may serve both the replacement and new construction markets, allow us to compete effectively in these markets.

Acquisition Strategy

We focus on acquiring businesses that either complement our current presence in existing markets or establish a presence in new geographic markets. Since 1989, we have acquired 59 HVAC/R distribution businesses, six of which currently operate as primary operating subsidiaries. The other smaller acquired distributors have been integrated into or are under the management of our primary operating subsidiaries. Through a combination of sales and market share growth, opening of new locations, tuck-in acquisitions, expansion of product lines, improved pricing and programs that have resulted in higher gross profit, performance incentives and a culture of equity value for key leadership, we have produced substantial sales and earnings growth post-acquisition. We continue to pursue additional strategic acquisitions and/or joint ventures to allow further penetration in existing markets and expansion into new geographic markets.

Product Line Expansion

We actively seek new or expanded territories of distribution from our key equipment suppliers. We currently maintain significant relationships with Carrier, Rheem, Goodman and Nordyne. We continually evaluate new parts and supply products to support equipment sales and further enhance service to our customers. This initiative includes increasing the product offering with existing vendors and identifying new product opportunities through traditional and non-traditional supply channels. We have also introduced private-label products as a means to obtain market share and grow revenues. We believe that our private-label branded products complement our existing product offerings at selected locations, based on customer needs and the particular market position and price of these products.

Operating Philosophy

We encourage our acquired subsidiaries to operate in a manner that builds upon the long-term relationships they have established between their suppliers and customers. Typically, we maintain the identity and culture of acquired businesses by retaining their historical trade names, management teams and sales organizations and continuing their product brand-name offerings. We believe this strategy allows us to build on the value of the acquired operations by creating additional sales opportunities while providing an attractive exit strategy for the former owners of these companies.

We maintain a specialized staff at our corporate headquarters that provides functional support for our subsidiaries' growth strategies in their respective markets. Such functional support staff includes specialists in finance, accounting, product procurement, information technology, treasury and working capital management, tax planning, risk management and safety. Certain general and administrative expenses are targeted for cost savings by leveraging the overall business volume and improving operating efficiencies.

Technology

Our technology initiatives include: (i) the development of mobile applications for iOS and Android devices focused on helping our customers operate more efficiently and interact with our locations more easily; (ii) implementing effective point-of-sale systems that allow timely and effective customer service, including up-to-date pricing, credit checks, credit card processing and inventory availability; (iii) enabling connectivity with our suppliers; (iv) enabling e-commerce between our customers and the relevant components of our subsidiaries' business software; and (v) maintaining our website, ACDocor.com, which educates consumers about energy efficient HVAC solutions and financial incentives related to the installation of energy efficient systems and connects them with high quality contractors.

DESCRIPTION OF BUSINESS

Products

We sell an expansive line of products and maintain a diverse mix of inventory to meet our customers' immediate needs and seek to provide products a contractor would generally require when installing or repairing a central air conditioner, furnace or refrigeration system on short notice. The cooling capacity of air conditioning units is measured in tons. One ton of cooling capacity is equivalent to 12,000 British Thermal Units ("BTUs") and is generally adequate to air condition approximately 500 square feet of residential space. The products we distribute consist of: (i) equipment, including residential central air

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conditioners ranging from 1-1/2 to 5 tons, gas, electric and oil furnaces ranging from 50,000 to 150,000 BTUs, commercial air conditioning and heating equipment and systems ranging from 1-1/2 to 25 tons and other specialized equipment, (ii) parts, including replacement compressors, evaporator coils, motors and other component parts and (iii) supplies, including thermostats, insulation material, refrigerants, ductwork, grills, registers, sheet metal, tools, copper tubing, concrete pads, tape, adhesives and other ancillary supplies.

Sales of HVAC equipment accounted for 64% and 63% of our revenues for the years ended December 31, 2013 and 2012, respectively. Sales of other HVAC products (currently sourced from more than 1,300 vendors) comprised 31% and 33% of our revenues for the years ended December 31, 2013 and 2012, respectively. Sales of commercial refrigeration products accounted for 5% and 4% of our revenues for the years ended December 31, 2013 and 2012, respectively.

Distribution and Sales

At December 31, 2013, we operated from 569 locations, a vast majority of which are located in regions that we believe have demographic trends favorable to our business. We maintain large inventories at each of our warehouse locations, and either deliver products to customers using one of our 634 trucks or a third party logistics provider, or we make products available for pick-up at the location nearest to the customer. We have approximately 990 commissioned salespeople, averaging more than 10 years of experience in the HVAC/R distribution industry.

The markets we serve are as follows:

	% of Revenues for the Year Ended December 31, 2013	Number of Locations as of December 31, 2013
United States	85%	515
Canada	9%	36
Puerto Rico, Latin America and the Caribbean	3%	8
Mexico	3%	10
Total	100%	569

The largest market we serve is the United States, in which the most significant markets for HVAC/R products are in the Sun Belt. Accordingly, the majority of our distribution locations are in the Sun Belt, with the highest concentration in Florida and Texas. These markets have been a strategic focus of ours given their size, the reliance by homeowners and businesses on HVAC/R products to maintain a comfortable indoor environment and the population growth in these areas over the last 40 years, which has led to a substantial installed base requiring replacement, a shorter useful life for equipment given the hours of operation and the focus by electrical utilities on consumer incentives designed to promote replacement of HVAC/R equipment in an effort to improve energy efficiency.

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[Markets](#)

The table below identifies the number of our stores in the United States by location as of December 31, 2013:

Florida	105
Texas	87
California	37
North Carolina	37
Georgia	36
South Carolina	30
Virginia	22
Tennessee	21
Louisiana	18
New York	12
Mississippi	11
Massachusetts	10
Alabama	9
Maryland	8
Arizona	7
Kansas	7
Missouri	7
Arkansas	6
Connecticut	6
Oklahoma	5
Utah	5
New Jersey	4
Maine	3
Iowa	2
Kentucky	2
Nebraska	2
Nevada	2
Pennsylvania	2
Rhode Island	2
South Dakota	2
Colorado	1
Illinois	1
Indiana	1
New Hampshire	1
New Mexico	1
North Dakota	1
Vermont	1
West Virginia	1
Total	<u>515</u>

[Joint Ventures with Carrier Corporation](#)

In 2009, we formed a joint venture with Carrier, which we refer to as Carrier Enterprise I, in which Carrier contributed 95 of its company-owned locations in 13 Sun Belt states and Puerto Rico and its export division in Miami, Florida, and we contributed 15 locations that distributed Carrier products. On July 2, 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our ownership interest to 70%. We have an option to purchase from Carrier an additional 10% interest in Carrier Enterprise I, which becomes exercisable in July 2014.

In 2011, we formed a second joint venture with Carrier and completed two additional transactions. In April 2011, Carrier contributed 28 of its company-owned locations in eight Northeast U.S. states, and we contributed 14 locations in the Northeast United States. In July 2011, we purchased Carrier's distribution operations in Mexico, which included seven locations. Collectively, the Northeast locations and the Mexico operations are referred to as Carrier Enterprise II. We have a 60% controlling interest in Carrier Enterprise II, and Carrier has a 40% noncontrolling interest. Neither we nor Carrier has any options to purchase additional ownership interests in Carrier Enterprise II.

In 2012, we formed a third joint venture, which we refer to as Carrier Enterprise III, with UTC Canada Corporation, referred to as UTC Canada, an affiliate of Carrier. Carrier contributed 35 of its company-owned locations in Canada to Carrier Enterprise III. We have a 60% controlling interest in Carrier Enterprise III, and UTC Canada has a 40% noncontrolling interest. Neither we nor UTC Canada has any options to purchase additional ownership interests in Carrier Enterprise III.

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Combined, the joint ventures with Carrier represented 61% of our revenues in 2013. See *Supplier Concentration* in “Business Risk Factors” in Item 1A.

The business and affairs of the joint ventures are controlled, directed and managed exclusively by Carrier Enterprise I’s, Carrier Enterprise II’s and Carrier Enterprise III’s respective boards of directors (the “Boards”) pursuant to related operating agreements. The Boards have full, complete and exclusive authority, power and discretion to manage and control the business, property and affairs of their respective joint ventures and to make all decisions regarding those matters and to perform activities customary or incident to the management of such joint ventures, including approval of distributions to us, Carrier and UTC Canada. Each Board is composed of five directors, of whom three directors represent our controlling interest and two directors represent Carrier’s noncontrolling interest. Matters presented to the Boards for vote are considered approved or consented to upon the receipt of the affirmative vote of at least a majority of all directors entitled to vote with the exception of certain governance matters, which require joint approval.

Customers and Customer Service

Air conditioning and heating contractors and dealers that install HVAC/R products in homes and businesses must be licensed given the highly-regulated nature of the products, refrigerant, natural gas and building and zoning requirements. We currently serve more than 50,000 contractors and dealers who service the replacement and new construction markets for residential and light commercial central air conditioning, heating and refrigeration systems. No single customer in 2013, 2012 or 2011 represented more than 1% of our consolidated revenues. We focus on providing products where and when the customer needs them, technical support by phone or on site as required, and quick and efficient service at our locations. Increased customer convenience is also provided through mobile applications and e-commerce, which allows customers to access information online 24 hours a day, seven days a week to search for desired products, verify inventory availability, obtain pricing, place orders, check order status, schedule pickup or delivery times and make payments. We believe we compete successfully with other distributors primarily on the basis of an experienced sales organization, strong service support, maintenance of well-stocked inventories, and density of warehouse locations, high quality reputation, broad product lines and the ability to foresee customer demand for new products.

Key Suppliers

We have significant relationships with Carrier, Rheem, Goodman, Nordyne, Emerson, Manitowoc and DuPont, each of which is a leading manufacturer of HVAC/R products in the United States. Each manufacturer has a well-established reputation for producing high-quality, competitively-priced products. The manufacturers’ current product offerings, quality, serviceability and brand-name recognition allow us to operate favorably relative to our competitors. To maintain brand-name recognition, the manufacturers of air conditioning and heating equipment provide national advertising and participate with us in cooperative advertising programs and promotional incentives that are targeted to both dealers and end-users. We estimate that the replacement market for air conditioning products currently accounts for approximately 85% of industry sales in the United States, and we expect this percentage to increase as units installed in the past 20 years wear out or it otherwise becomes practical to replace older units with newer, more energy-efficient models.

Approximately 73%, 72% and 71% of our purchases in 2013, 2012 and 2011, respectively, were from the four key HVAC/R equipment suppliers. Our largest supplier, Carrier and its affiliates, accounted for 59%, 57% and 54% of all purchases made in 2013, 2012 and 2011, respectively. A significant interruption by Carrier, or the other suppliers, in the delivery of products could impair our ability to maintain current inventory levels and could adversely affect our financial results. Future financial results are also materially dependent upon the continued market acceptance of these manufacturers’ products and their ability to continue to manufacture products that comply with laws relating to environmental and efficiency standards. See “Business Risk Factors” in Item 1A.

Distribution Agreements

We have entered into distribution agreements with several of our key suppliers either on an exclusive or non-exclusive basis for terms generally ranging from one to ten years. Certain of the distribution agreements contain provisions that restrict or limit the sale of competitive products in the geographic markets served. Other than in the geographic markets where such restrictions and limitations apply, we may distribute other manufacturers’ lines of air conditioning or heating equipment.

We maintain separate and distinct trade name and distribution agreements with Carrier. These agreements provide us the use of various Carrier brand names and distribution rights for certain Carrier HVAC brands and products on an exclusive basis in specified territories. The trade name and distribution agreements are not subject to a stated term or expiration date. See *Supplier Concentration* in “Business Risk Factors” in Item 1A.

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Seasonality

Sales of residential central air conditioners, heating equipment and parts and supplies have historically been seasonal. Furthermore, profitability can be impacted favorably or unfavorably based on the severity or mildness of weather patterns during summer or winter selling seasons. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters, and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly even during the year except for dependence on housing completions and related weather and economic conditions.

Competition

We operate in highly competitive environments. We compete with a number of distributors and also with several air conditioning and heating equipment manufacturers that distribute a significant portion of their products through their own distribution organizations in certain markets. Competition within any given geographic market is based upon product availability, customer service, price and quality. Competitive pressures or other factors could cause our products or services to lose market acceptance or result in significant price erosion, all of which would have a material adverse effect on our results of operations, cash flows and liquidity.

Employees

We had approximately 4,800 employees as of December 31, 2013, substantially all of whom are non-union employees. Most of these employees are employed on a full-time basis, and our relations with our employees are good.

Order Backlog

Order backlog is not a material aspect of our business, and no material portion of our business is subject to government contracts.

Government Regulations, Environmental and Health and Safety Matters

Our business is subject to federal, state and local laws and regulations relating to the storage, handling, transportation and release of hazardous materials into the environment. These laws and regulations include the Clean Air Act, relating to minimum energy efficiency standards of HVAC systems and the production, servicing and disposal of certain ozone-depleting refrigerants used in such systems, including those established at the Montreal Protocol in 1992 concerning the phase-out of the production of CFC-based refrigerants on January 1, 2010 for use in new equipment. We are also subject to regulations concerning the transport of hazardous materials, including regulations adopted pursuant to the Motor Carrier Safety Act of 1990. Our operations are also subject to health and safety requirements including the Occupational, Safety and Health Act. We believe that the business is operated in compliance with all applicable federal, state and local provisions relating to the protection of the environment, transport of hazardous materials and health and safety requirements. In addition, we could be affected by future laws or regulations imposed in response to concerns over climate change.

Financial Information About Geographic Areas

Our operations are primarily within the United States and Puerto Rico. Products are sold on an export-only basis to portions of Latin America and the Caribbean Basin. The following tables set forth revenues and long-lived assets by geographic area (in millions):

<i>Years Ended December 31,</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Revenues:			
United States	\$3,325	\$3,088	\$2,939
Canada	318	240	—
Mexico	100	104	39
Total Revenues	<u>\$3,743</u>	<u>\$3,432</u>	<u>\$2,978</u>
<i>December 31,</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Long-Lived Assets:			
United States	\$ 429	\$ 429	\$ 430
Canada	208	225	—
Mexico	5	5	4
Total Long-Lived Assets	<u>\$ 642</u>	<u>\$ 659</u>	<u>\$ 434</u>

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Revenues are attributed to countries based on the location of the store from which the sale occurred. Long-lived assets consist of property and equipment, goodwill and intangible assets.

Available Information

Our website is at www.watsco.com. Our investor relations website is located at www.investors.watsco.com. We promptly make available, free of charge, on our investor relations website under the heading "SEC Filings" our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed with or furnished to the Securities and Exchange Commission pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended. The reference to our website address does not constitute incorporation by reference of the information contained on our website and none of such information is part of this report.

ITEM 1A. RISK FACTORS

Business Risk Factors

Supplier Concentration

Our purchases from Carrier and its affiliates comprised 59% of all purchases made during 2013. Significant relationships currently exist with four of the seven major HVAC equipment manufacturers; and purchases from these equipment suppliers, including Carrier, comprised 73% of all purchases made in 2013. Given the significant concentration of our supply chain, particularly with Carrier, any significant interruption by the manufacturers or a termination of a distribution agreement could temporarily disrupt the operations of certain subsidiaries. Additionally, our operations are materially dependent upon the continued market acceptance of these manufacturers' products and their ability to continue to manufacture products that are competitive and that comply with laws relating to environmental and efficiency standards. Our inability to obtain products from one or more of these manufacturers or a decline in market acceptance of these manufacturers' products could have a material adverse effect on our results of operations, cash flows and liquidity.

We maintain separate and distinct trade name distribution agreements with Carrier. These agreements provide us the use of various Carrier brand names and distribution rights for certain Carrier HVAC brands and products on an exclusive basis in specified territories. The trade name and distribution agreements are not subject to a stated term or expiration date.

We also maintain distribution agreements with our other key equipment suppliers, either on an exclusive or non-exclusive basis, for terms generally ranging from one to ten years. Certain of the distribution agreements contain provisions that restrict or limit the sale of competitive products in the markets served. Other than the markets where such restrictions and limitations may apply, we may distribute other manufacturers' lines of air conditioning or heating equipment.

Risks Inherent in Acquisitions

As part of our strategy, we intend to pursue additional acquisitions of complementary businesses. If we complete future acquisitions and/or joint ventures, we may be required to incur or assume additional debt and/or issue additional shares of our common stock as consideration, which will dilute our existing shareholders' ownership interest in us and may affect our results of operations. Growth through acquisitions involves a number of risks, including, but not limited to, the following:

- the ability to identify and consummate transactions with complementary acquisition candidates;
- the successful operation and/or integration of acquired companies;
- diversion of management's attention from other daily functions;
- issuance by us of equity securities that would dilute ownership of our existing shareholders;
- incurrence and/or assumption of significant debt and contingent liabilities; and
- possible loss of key employees and/or customer relationships of the acquired companies.

In addition, acquired companies may have liabilities that we failed, or were unable, to discover in the course of performing due diligence investigations. We cannot assure you that the indemnification granted to us by sellers of acquired companies will be sufficient in amount, scope or duration to offset the possible liabilities associated with businesses or properties that we assume upon consummation of an acquisition. Any such liabilities, individually or in the aggregate, could have a material adverse effect on our business.

Failure to successfully manage the operational challenges and risks associated with, or resulting from, acquisitions could adversely affect our results of operations, cash flows and liquidity.

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Competition

We operate in highly competitive environments. We compete with a number of distributors and also with several air conditioning and heating equipment manufacturers that distribute a significant portion of their products through their own distribution organizations in certain markets. Competition within any given geographic market is based upon product availability, customer service, price and quality. Competitive pressures or other factors could cause our products or services to lose market acceptance or result in significant price erosion, all of which would have a material adverse effect on our results of operations, cash flows and liquidity.

Decline in Economic Conditions

The global and United States economy experienced a significant contraction in 2008, including sharply reduced availability of business and consumer credit. We rely on the capital markets as well as the credit markets to meet our financial commitments and short-term liquidity needs if internal funds are not available from our operations. Our access to funds under our line of credit is dependent on the ability of the syndicate banks to meet their respective funding commitments. Disruptions in the capital and credit markets could adversely affect our ability to draw on our line of credit and may also affect the determination of certain interest rates, particularly rates based on LIBOR, which is one of the base rates under our line of credit. Any disruptions in these markets could result in increased borrowing costs and/or reduced borrowing capacity under our line of credit. Any long-term disruption could require that we take measures to conserve cash until the markets stabilize or until alternative credit arrangements or other funding for our business needs can be arranged. Such measures could include reducing or eliminating dividend payments, deferring capital expenditures and reducing or eliminating discretionary uses of cash.

A decline in economic conditions and lack of availability of business and consumer credit could have an adverse effect on our business and results of operations. Any capital and credit market disruption could cause broader economic downturns, which may lead to reduced demand for our products and increased incidence of customers' inability to pay their accounts. Further, bankruptcies or similar events by customers may cause us to incur bad debt expense at levels higher than historically experienced. Also, our suppliers may be negatively impacted by deteriorating economic conditions, causing disruption or delay of product availability. These events would adversely impact our results of operations, cash flows and financial position. Additionally, if the conditions of the capital and credit markets adversely affect the financial institutions that have committed to extended credit to us, they may be unable to fund borrowings under such commitments, which could have an adverse impact on our financial condition, liquidity and our ability to borrow funds, if needed, for working capital, acquisitions, capital expenditures and other corporate purposes.

Seasonality

Sales of residential central air conditioners, heating equipment and parts and supplies have historically been seasonal. Furthermore, profitability can be impacted favorably or unfavorably based on the severity or mildness of weather patterns during summer or winter selling seasons. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters, and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly even during the year except for dependence on housing completions and related weather and economic conditions.

Dependence on Key Personnel

Much of our success has depended on the skills, experience and services of senior management personnel. The loss of any of our executive officers or other key senior management personnel could harm our business. We must continue to recruit, retain and motivate management and other employees sufficiently in order to both maintain our current business and to execute our strategic initiatives. Our success has also substantially depended on the contributions and abilities of our store employees whom we rely on to give customers a superior in-store experience. Accordingly, our performance depends on our ability to recruit and retain high quality employees to work in and manage our stores. If we are unable to recruit, retain and motivate employees sufficiently in order to maintain our current business and support our projected growth and expansion, our business and financial performance may be adversely affected.

Foreign Currency Exchange Rate Fluctuations

The functional currency of our operations in Canada is the Canadian dollar and the functional currency of our operations in Mexico is the U.S. dollar because the majority of our Mexican transactions are denominated in U.S. dollars. Foreign currency exchange rates and fluctuations may have an impact on transactions denominated in Canadian dollars and Mexican Pesos, and, therefore, could adversely affect our financial performance.

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International Political Risk

Our international sales and operations are subject to various risks associated with changes in local laws, regulations and policies, including those related to tariffs, trade restrictions and trade agreements, investments, taxation, capital controls, employment regulations, different liability standards and limitations on the repatriation of funds due to foreign currency controls. Our international sales and operations are also sensitive to changes in foreign national priorities, including government budgets, as well as political and economic instability. Unfavorable changes in any of the foregoing could adversely affect our results of operations. Additionally, failure to comply with the U.S. Foreign Corrupt Practices Act could subject us to, among other things, penalties and legal expenses that could harm our reputation and have a material adverse effect on our business, financial condition and results of operations.

General Risk Factors

Goodwill and Intangibles

At December 31, 2013, goodwill and intangibles represented approximately 36% of our total assets. The recoverability of goodwill and indefinite lived intangibles is evaluated at least annually and when events or changes in circumstances indicate that the carrying amounts may not be recoverable. The identification and measurement of goodwill impairment involves the estimation of the fair value of our reporting unit and contains uncertainty because management must use judgment in determining appropriate assumptions to be used in the measurement of fair value. The estimates of fair value of our reporting unit and indefinite lived intangibles are based on the best information available as of the date of the assessment and incorporates management's assumptions about expected future cash flows and contemplates other valuation techniques. Future cash flows can be affected by changes in the industry, a declining economic environment or market conditions. We cannot assure you that we will not suffer material impairments to goodwill in the future.

Risks Related to Insurance Coverage

We carry general liability, comprehensive property damage, workers' compensation, health benefits and other insurance coverage that management considers adequate for the protection of its assets and operations. There can be no assurance, however, that the coverage limits of such policies will be adequate to cover losses and expenses for lawsuits brought or which may be brought against us. A loss in excess of insurance coverage could have a material adverse effect on our financial position and/or profitability. Certain self-insurance risks for casualty insurance programs and health benefits are retained and reserves are established based on claims filed and estimates of claims incurred but not yet reported. Assurance cannot be provided that actual claims will not exceed present estimates. Exposure to catastrophic losses has been limited by maintaining excess and aggregate liability coverage and implementing stop-loss control programs.

Control by Existing Shareholder

As of December 31, 2013, Albert H. Nahmad, our Chairman and Chief Executive Officer, a limited partnership and various trusts controlled by him, collectively had beneficial ownership of approximately 52% of the combined voting power of our outstanding Common and Class B common stock. Based on Mr. Nahmad's stock ownership and the stock ownership of the limited partnership and various trusts controlled by him, Mr. Nahmad has the voting power to elect all but three members of our nine-person Board of Directors and to control most corporate actions requiring shareholder approval.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our main properties include warehousing and distribution facilities, trucks and administrative office space.

Warehousing and Distribution Facilities

At December 31, 2013, we operated 569 warehousing and distribution facilities across 38 U.S. states, Canada, Mexico and Puerto Rico, having an aggregate of approximately 13.0 million square feet of space, of which approximately 12.7 million square feet is leased. The majority of these leases are for terms of three to five years. We believe that our facilities are sufficient to meet our present operating needs.

Trucks

At December 31, 2013, we operated 634 ground transport vehicles, including delivery and pick-up trucks, vans and tractors. Of this number, 317 trucks were leased and the rest were owned. We believe that the present size of our truck fleet is adequate to support our operations.

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Administrative Facility

Senior management and support staff are located at our corporate headquarters in Miami, Florida in approximately 8,900 square feet of owned space.

ITEM 3. LEGAL PROCEEDINGS

Information with respect to this item may be found in Note 14 to our audited consolidated financial statements contained in this Annual Report on Form 10-K under the caption "Litigation, Claims and Assessments," which information is incorporated herein by reference.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Stock Exchange Information, Common Share Price Performance and Dividends

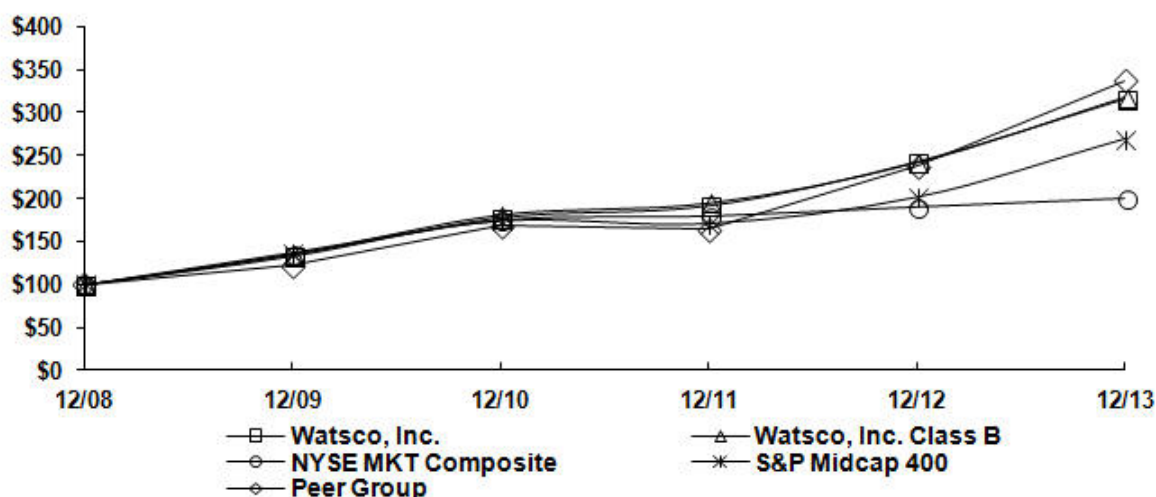
Our Common stock is listed on the New York Stock Exchange and the Professional Segment of NYSE Euronext in Paris under the ticker symbol WSO and our Class B common stock is listed on the New York Stock Exchange under the ticker symbol WSOB.

Our 2013 Annual Report contains “Information on Common Stock,” which identifies the exchanges on which our two classes of common stock are traded and contains the high and low sales prices and dividend information for the years ended December 31, 2013 and 2012, and is incorporated herein by reference.

Shareholder Return Performance

The following graph compares the cumulative five-year total return attained by holders of our Common stock and Class B common stock relative to the cumulative total returns of the NYSE MKT Composite index, the S&P MidCap 400 index and a customized peer group of companies, which are: Beacon Roofing Supply, Inc., Lennox International Inc., Pool Corp and WESCO International, Inc. An investment of \$100 (with reinvestment of all dividends) is assumed to have been made in our common stock, in each index and in the peer group on December 31, 2008 and its relative performance is tracked through December 31, 2013.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*
Among Watsco, Inc., the NYSE MKT Composite Index, the S&P Midcap 400 Index and a Peer Group



*\$100 invested on 12/31/08 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

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	12/08	12/09	12/10	12/11	12/12	12/13
Watsco, Inc.	100.00	133.29	177.97	191.77	242.73	315.48
Watsco, Inc. Class B	100.00	135.26	180.94	194.48	241.23	317.00
NYSE MKT Composite	100.00	135.53	175.07	179.96	190.69	200.56
S&P MidCap 400	100.00	137.38	173.98	170.96	201.53	269.04
Peer Group	100.00	122.44	168.33	164.20	237.46	337.01

[Table of Contents](#)**Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

The following table provides information with respect to purchases we made of our common stock during the quarter ended December 31, 2013:

Period	Issuer Purchases of Equity Securities			Maximum Number of Shares that May Yet be Purchased under the Program (1)
	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	
October 1 – October 31	7,779(2)	\$ 94.75(2)	—	1,129,087
November 1 – November 30	—	—	—	1,129,087
December 1 – December 31	—	—	—	1,129,087
Total	7,779	\$ 94.75	—	1,129,087

- (1) In September 1999, our Board of Directors authorized the repurchase, at management's discretion, of up to 7,500,000 shares of common stock in the open market or via private transactions. No shares were repurchased under this plan in 2013, 2012 or 2011.
- (2) Reflects shares of Common stock delivered to us by participants in our 2001 Incentive Compensation Plan as payment for the exercise price of options and related tax withholdings in accordance with awards granted thereunder.

Dividends

Cash dividends per share of \$1.15, \$7.48 and \$2.23 for both Common and Class B common stock were paid in 2013, 2012 and 2011, respectively. Future dividends will be declared and paid at the sole discretion of the Board of Directors and will depend upon such factors as cash flow generated by operations, profitability, financial condition, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

ITEM 6. SELECTED FINANCIAL DATA

Our 2013 Annual Report contains "Selected Consolidated Financial Data", which section is incorporated herein by reference.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our 2013 Annual Report contains "Management's Discussion and Analysis of Financial Condition and Results of Operations", which section is incorporated herein by reference.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our 2013 Annual Report contains "Quantitative and Qualitative Disclosures about Market Risk", which section is incorporated herein by reference.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our 2013 and 2012 Consolidated Balance Sheets and other consolidated financial statements for the years ended December 31, 2013, 2012 and 2011, together with the report thereon of KPMG LLP dated February 27, 2014 in our 2013 Annual Report are incorporated herein by reference.

The 2013 and 2012 unaudited Selected Quarterly Financial Data appearing in our 2013 Annual Report is incorporated herein by reference.

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (“the Exchange Act”)) that are, among other things, designed to ensure that information required to be disclosed by us under the Exchange Act is accumulated and communicated to management, including our Chief Executive Officer (“CEO”), Senior Vice President (“SVP”) and Chief Financial Officer (“CFO”), to allow for timely decisions regarding required disclosure and appropriate SEC filings.

Our management, with the participation of our CEO, SVP and CFO, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, and, based on that evaluation, our CEO, SVP and CFO concluded that our disclosure controls and procedures were effective, at a reasonable assurance level, at and as of such date.

Management’s Report on Internal Control over Financial Reporting

Our 2013 Annual Report contains “Management’s Report on Internal Control over Financial Reporting” and the report thereon of KPMG LLP dated February 27, 2014, and each is incorporated herein by reference.

Changes in Internal Control over Financial Reporting

We are continuously seeking to improve the efficiency and effectiveness of our operations and of our internal controls. This results in refinements to processes throughout the Company. However, there were no changes in internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2013, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

This part of Form 10-K, which includes Items 10 through 14, is omitted because we will file definitive proxy material pursuant to Regulation 14A not more than 120 days after the close of our most recently ended fiscal year, which proxy material will include the information required by Items 10 through 14 and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

- (a) (1) Financial Statements. Our consolidated financial statements are incorporated by reference from our 2013 Annual Report.
- (2) Financial Statement Schedules. The schedules are omitted because they are not applicable or the required information is shown in the consolidated financial statements or notes thereto.
- (3) Exhibits. The following exhibits are submitted with this Annual Report on Form 10-K or, where indicated, incorporated by reference to other filings.
- 3.1 Composite Articles of Incorporation of Watsco, Inc. (filed as Exhibit 3.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012 and incorporated herein by reference).
- 3.2 Watsco Inc. Amended and Restated Bylaws effective August 22, 2012 (filed as Exhibit 3.1 to the Current Report on Form 8-K on August 28, 2012 and incorporated herein by reference).
- 4.1 Specimen form of Class B Common Stock Certificate (filed as Exhibit 4.6 to the Registration Statement on Form S-1 (No. 33-56646) and incorporated herein by reference).

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- 4.2 Specimen form of Common Stock Certificate (filed as Exhibit 4.4 to the Annual Report on Form 10-K for the fiscal year ended December 31, 1994 and incorporated herein by reference).
- 10.1(a) Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.20 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 1996 and incorporated herein by reference). *
- 10.1(b) First Amendment dated January 1, 2001 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.13 to the Annual Report on Form 10-K for the year ended December 31, 2000 and incorporated herein by reference). *
- 10.1(c) Second Amendment dated January 1, 2002 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.15 to the Annual Report on Form 10-K for the year ended December 31, 2001 and incorporated herein by reference). *
- 10.1(d) Third Amendment dated January 1, 2003 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.11 to the Annual Report on Form 10-K for the year ended December 31, 2002 and incorporated herein by reference). *
- 10.1(e) Fourth Amendment dated January 1, 2004 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2004 and incorporated herein by reference). *
- 10.1(f) Fifth Amendment dated January 1, 2005 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 and incorporated herein by reference). *
- 10.1(g) Sixth Amendment dated January 1, 2006 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.16 to the Annual Report on Form 10-K for the year ended December 31, 2005 and incorporated herein by reference). *
- 10.1(h) Seventh Amendment dated January 1, 2007 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.18 to the Annual Report on Form 10-K for the year ended December 31, 2006 and incorporated herein by reference). *
- 10.1(i) Eighth Amendment dated January 1, 2008 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2008 and incorporated herein by reference). *
- 10.1(j) Ninth Amendment dated December 10, 2008 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.19 to the Annual Report on Form 10-K for the year ended December 31, 2008 and incorporated herein by reference). *
- 10.1(k) Tenth Amendment dated January 1, 2009 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2009 and incorporated herein by reference). *
- 10.1(l) Eleventh Amendment dated January 1, 2010 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 and incorporated herein by reference). *
- 10.1(m) Twelfth Amendment dated January 1, 2011 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2011 and incorporated herein by reference). *
- 10.1(n) Thirteenth Amendment dated January 1, 2012 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2012 and incorporated herein by reference). *
- 10.1(o) Fourteenth Amendment dated January 1, 2013 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 and incorporated herein by reference). *

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- 10.2 Watsco, Inc. Amended and Restated 2001 Incentive Compensation Plan (filed as Appendix A to the Definitive Proxy Statement on Schedule 14A in respect of our 2009 Annual Meeting of Shareholders and incorporated herein by reference). *
- 10.3 Fourth Amended and Restated 1996 Qualified Employee Stock Purchase Plan dated April 18, 2011 (filed as Appendix A to the Definitive Proxy Statement on Schedule 14A in respect of our 2011 Annual Meeting of Shareholders and incorporated herein by reference). *
- 10.4(a) Credit Agreement dated as of April 27, 2012, by and among Watsco, Inc., as Borrower, Watsco Canada, Inc., as Canadian Borrower, the Lenders from time to time party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and Collateral Agent, Bank of America, N.A. and Wells Fargo Bank, National Association as Co-Syndication Agents and U.S. Bank National Association as Documentation Agent (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q on August 2, 2013 and incorporated herein by reference).
- 10.4(b) Amendment No. 1 dated as of August 8, 2012, to the Credit Agreement dated as of April 27, 2012 (filed as Exhibit 10.4(b) to the Annual Report on Form 10-K for the year ended December 31, 2012, filed on February 28, 2013 and incorporated herein by reference).
- 10.4(c) Amendment No. 2, dated as of July 1, 2013, to Credit Agreement dated as of April 27, 2012, by and among Watsco, Inc., as Borrower, Watsco Canada, Inc., as Canadian Borrower, the Lenders from time to time party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and Collateral Agent, Bank of America, N.A. and Wells Fargo Bank, National Association as Co-Syndication Agents and U.S. Bank National Association as Documentation Agent (filed as Exhibit 10.1 to the Current Report on Form 8-K on July 2, 2013 and incorporated herein by reference).
- 10.5(a) Purchase and Contribution Agreement dated May 3, 2009 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.1 to the Current Report on Form 8-K on May 7, 2009 and incorporated herein by reference).
- 10.5(b) Amendment to Purchase and Contribution Agreement dated as of June 29, 2009 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.2 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).
- 10.6 Operating Agreement of Carrier Enterprise, LLC (Amended and Restated), dated as of July 1, 2009 (filed as Exhibit 10.2 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).
- 10.7(a) Shareholder Agreement by and between Watsco, Inc. and Carrier Corporation, dated as of July 1, 2009 (filed as Exhibit 10.3 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).
- 10.7(b) Amended and Restated Shareholder Agreement by and between Watsco, Inc. and Carrier Corporation, dated as of January 24, 2012 (filed as Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2011 and incorporated herein by reference).
- 10.7(c) Second Amended and Restated Shareholder Agreement by and among Watsco, Inc., Carrier Corporation and UTC Canada Corporation, dated as of April 27, 2012 (filed as Exhibit 10.4 to the Current Report on Form 8-K on May 3, 2012 and incorporated herein by reference).
- 10.8 Purchase and Contribution Agreement dated March 18, 2011 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.1 to the Current Report on Form 8-K on March 24, 2011 and incorporated herein by reference).
- 10.9 Operating Agreement of Carrier Enterprise Northeast, LLC, dated as of April 30, 2011 (filed as Exhibit 10.29 to the Annual Report on Form 10-K for the year ended December 31, 2011 and incorporated herein by reference).
- 10.10 Asset Purchase Agreement dated March 13, 2012 by and between UTC Canada Corporation, Watsco, Inc., Watsco Canada, Inc. and Carrier Enterprise Canada, L.P. (filed as Exhibit 2.1 to the Current Report on Form 8-K on March 14, 2012 and incorporated herein by reference).
- 10.11 Carrier Enterprise Canada (G.P.), Inc. Shareholders' Agreement dated as of April 27, 2012 (filed as Exhibit 10.2 to the Current Report on Form 8-K on May 3, 2012 and incorporated herein by reference).

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10.12	Subscription Agreement dated March 13, 2012 by and between Watsco, Inc., UTC Canada Corporation and Carrier Corporation (filed as Exhibit 10.1 to the Current Report on Form 8-K on March 14, 2012 and incorporated herein by reference).
13	2013 Annual Report to Shareholders (with the exception of the information incorporated by reference into Items 1, 5, 6, 7 and 8 of this Form 10-K, the 2013 Annual Report to Shareholders is provided solely for the information of the SEC and is not deemed “filed” as part of this Form 10-K). #
21.1	Subsidiaries of the Registrant. #
23.1	Consent of Independent Registered Public Accounting Firm – KPMG LLP. #
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
31.2	Certification of Senior Vice President pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
31.3	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
32.1	Certification of Chief Executive Officer, Senior Vice President and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. +
101.INS	XBRL Instance Document. #
101.SCH	XBRL Taxonomy Extension Schema Document. #
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document. #
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document. #
101.LAB	XBRL Taxonomy Extension Label Linkbase Document. #
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document. #

filed herewith.

+ furnished herewith.

* Management contract or compensation plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WATSCO, INC.

February 27, 2014

By: /s/ Albert H. Nahmad
Albert H. Nahmad, President

February 27, 2014

By: /s/ Ana M. Menendez
Ana M. Menendez, Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>SIGNATURE</u>	<u>TITLE</u>	<u>DATE</u>
<u>/s/ ALBERT H. NAHMAD</u> Albert H. Nahmad	Chairman of the Board and Chief Executive Officer (principal executive officer)	February 27, 2014
<u>/s/ BARRY S. LOGAN</u> Barry S. Logan	Director and Senior Vice President	February 27, 2014
<u>/s/ ANA M. MENENDEZ</u> Ana M. Menendez	Chief Financial Officer (principal accounting officer and principal financial officer)	February 27, 2014
<u>/s/ CESAR L. ALVAREZ</u> Cesar L. Alvarez	Director	February 27, 2014
<u>/s/ DAVID C. DARNELL</u> David C. Darnell	Director	February 27, 2014
<u>/s/ DENISE DICKINS</u> Denise Dickins	Director	February 27, 2014
<u>/s/ STEVEN R. FEDRIZZI</u> Steven R. Fedrizzi	Director	February 27, 2014
<u>/s/ PAUL F. MANLEY</u> Paul F. Manley	Director	February 27, 2014
<u>/s/ AARON J. NAHMAD</u> Aaron J. Nahmad	Director and Vice President of Strategy and Innovation	February 27, 2014
<u>/s/ GEORGE P. SAPE</u> George P. Sape	Director	February 27, 2014

Exhibit Index

<u>Exhibit Number</u>	<u>Description</u>
13	2013 Annual Report to Shareholders (with the exception of the information incorporated by reference into Items 1, 5, 6, 7 and 8 of this Form 10-K, the 2013 Annual Report to Shareholders is provided solely for the information of the SEC and is not deemed “filed” as part of this Form 10-K).
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31.3	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer, Senior Vice President and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

WATSCO, INC. AND SUBSIDIARIES
SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with the consolidated financial statements, including the notes thereto, included under Item 8 of Part II, "Financial Statements and Supplementary Data," and the information contained in Item 7 of Part II, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Annual Report on Form 10-K for the year ended December 31, 2013.

<i>(In thousands, except per share data)</i>	<u>2013</u>	<u>2012 (1)</u>	<u>2011</u>	<u>2010</u>	<u>2009 (2)</u>
FOR THE YEAR					
Revenues	\$3,743,330	\$3,431,712	\$2,977,759	\$2,844,595	\$2,001,815
Gross profit	899,253	814,395	728,294	673,241	480,832
Operating income	271,209	224,908	199,050	165,572	81,060
Net income	187,719	157,601	137,742	111,722	51,573
Less: net income attributable to noncontrolling interest	59,996	54,267	47,292	30,962	8,259
Net income attributable to Watsco, Inc.	<u>\$ 127,723</u>	<u>\$ 103,334</u>	<u>\$ 90,450</u>	<u>\$ 80,760</u>	<u>\$ 43,314</u>
Diluted earnings per share for Common and Class B common stock	\$ 3.68	\$ 2.70	\$ 2.74	\$ 2.49	\$ 1.40
Cash dividends per share:					
Common stock	\$ 1.15	\$ 7.48	\$ 2.23	\$ 2.04	\$ 1.89
Class B common stock	\$ 1.15	\$ 7.48	\$ 2.23	\$ 2.04	\$ 1.89
Weighted-average Common and Class B common shares outstanding - Diluted	32,258	31,744	30,753	30,579	28,521
AT YEAR END					
Total assets	\$1,669,531	\$1,682,055	\$1,268,148	\$1,237,227	\$1,160,613
Total long-term obligations	\$ 230,557	\$ 316,196	\$ —	\$ 10,016	\$ 13,429
Total shareholders' equity	\$1,127,392	\$1,022,040	\$1,001,710	\$ 928,896	\$ 894,808
Number of employees	4,800	4,600	4,300	4,000	4,100

- (1) *On October 31, 2012, we paid a special dividend of \$5.00 per share of Common and Class B common stock that resulted in a \$0.33 per share reduction in diluted earnings per share.*
- (2) *Effective January 1, 2009, we adopted the provisions of accounting guidance stating that non-vested share-based payment awards that contain non-forfeitable rights to dividends are considered participating securities and should be included in the computation of earnings per share pursuant to the two-class method for all periods presented. We also adopted the provisions of revised accounting guidance for recognizing and measuring assets acquired and liabilities assumed in a business combination.*

WATSCO, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Annual Report on Form 10-K for the year ended December 31, 2013 contains or incorporates by reference statements that are not historical in nature and that are intended to be, and are hereby identified as, "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995, including statements regarding, among other items, (i) economic conditions, (ii) business and acquisition strategies, (iii) potential acquisitions and/or joint ventures, (iv) financing plans and (v) industry, demographic and other trends affecting our financial condition or results of operations. These forward-looking statements are based largely on management's current expectations and are subject to a number of risks, uncertainties and changes in circumstances, certain of which are beyond their control.

Actual results could differ materially from these forward-looking statements as a result of several factors, including, but not limited to:

- general economic conditions;
- competitive factors within the HVAC/R industry;
- effects of supplier concentration;
- fluctuations in certain commodity costs;
- consumer spending;
- consumer debt levels;
- new housing starts and completions;
- capital spending in the commercial construction market;
- access to liquidity needed for operations;
- seasonal nature of product sales;
- weather conditions;
- insurance coverage risks;
- federal, state and local regulations impacting our industry and products;
- prevailing interest rates;
- foreign currency exchange rate fluctuations;
- international political risk; and
- the continued viability of our business strategy.

In light of these uncertainties, there can be no assurance that the forward-looking information contained herein will be realized or, even if realized, in whole or in part, that the information will have the expected consequences to, or effects on, our business or operations. For additional information identifying other important factors that may affect our operations and could cause actual results to vary materially from those anticipated in the forward-looking statements, see our SEC filings, including but not limited to, the discussion included in Item 1A "Risk Factors" of this Annual Report on Form 10-K for the year ended December 31, 2013. Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information or the discussion of such risks and uncertainties to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information, except as required by applicable law.

The following information should be read in conjunction with the information contained in Item 1A, "Risk Factors" and the consolidated financial statements, including the notes thereto, included under Item 8, "Financial Statements and Supplementary Data" of this Annual Report on Form 10-K for the year ended December 31, 2013.

Company Overview

WatSCO, Inc. and its subsidiaries (collectively, "WatSCO," or "we", "us" or "our") was incorporated in Florida in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies ("HVAC/R") in the HVAC/R distribution industry. At December 31, 2013, we operated from 569 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean.

Revenues primarily consist of sales of air conditioning, heating and refrigeration equipment and related parts and supplies. Selling, general and administrative expenses primarily consist of selling expenses, the largest components of which are salaries, commissions and marketing expenses that are variable and correlate to changes in sales. Other significant selling, general and administrative expenses relate to the operation of warehouse facilities, including a fleet of trucks and forklifts and facility rent, which are payable mostly under non-cancelable operating leases.

Sales of residential central air conditioners, heating equipment and parts and supplies are seasonal. Furthermore, results of operations can be impacted favorably or unfavorably based on weather patterns during summer and winter selling seasons. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters, and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction market is fairly consistent during the year, subject to weather and economic conditions, including their effect on the number of housing completions.

Joint Ventures with Carrier Corporation

In 2009, we formed a joint venture with Carrier Corporation (“Carrier”), which we refer to as Carrier Enterprise I, in which Carrier contributed 95 of its company-owned locations in 13 Sun Belt states and Puerto Rico and its export division in Miami, Florida, and we contributed 15 locations that distributed Carrier products. On July 2, 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our ownership interest to 70%. We have an option to purchase from Carrier an additional 10% interest in Carrier Enterprise I, which becomes exercisable in July 2014.

In 2011, we formed a second joint venture with Carrier and completed two additional transactions. In April 2011, Carrier contributed 28 of its company-owned locations in eight Northeast U.S. states, and we contributed 14 locations in the Northeast U.S. In July 2011, we purchased Carrier’s distribution operations in Mexico, which included seven locations. Collectively, the Northeast locations and the Mexico operations are referred to as Carrier Enterprise II. We have a 60% controlling interest in Carrier Enterprise II, and Carrier has a 40% noncontrolling interest. Neither we nor Carrier has any options to purchase additional ownership interests in Carrier Enterprise II.

In 2012, we formed a third joint venture, which we refer to as Carrier Enterprise III, with UTC Canada Corporation, referred to as UTC Canada, an affiliate of Carrier. Carrier contributed 35 of its company-owned locations in Canada to Carrier Enterprise III. We have a 60% controlling interest in Carrier Enterprise III, and UTC Canada has a 40% noncontrolling interest. Neither we nor UTC Canada has any options to purchase additional ownership interests in Carrier Enterprise III.

Critical Accounting Policies

Management’s discussion and analysis of financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the reporting period. Actual results may differ from these estimates under different assumptions or conditions. At least quarterly, management reevaluates its judgments and estimates, which are based on historical experience, current trends and various other assumptions that are believed to be reasonable under the circumstances.

Our significant accounting policies are discussed in Note 1 to our consolidated financial statements included with this Annual Report on Form 10-K. Management believes that the following accounting policies include a higher degree of judgment and/or complexity and, thus, are considered to be critical accounting policies. Management has discussed the development and selection of critical accounting policies with the Audit Committee of the Board of Directors and the Audit Committee has reviewed the disclosures relating to them.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is maintained for estimated losses resulting from the inability of customers to make required payments. We typically do not require our customers to provide collateral. Accounting for doubtful accounts contains uncertainty because management must use judgment to assess the collectability of these accounts. When preparing these estimates, management considers a number of factors, including the aging of a customer’s account, past transactions with customers, creditworthiness of specific customers, historical trends and other information. Our business is seasonal and our customers’ businesses are also seasonal. Sales are lowest during the first and fourth quarters and past due accounts receivable balances as a percentage of total trade receivables generally increase during these quarters. We review our accounts receivable reserve policy periodically, reflecting current risks, trends and changes in industry conditions.

The allowance for doubtful accounts was \$5.7 million and \$10.5 million at December 31, 2013 and 2012, respectively, a decrease of \$4.8 million. Accounts receivable balances greater than 90 days past due as a percent of accounts receivable at December 31, 2013 decreased to 1.8% compared to 3.9% at December 31, 2012. These decreases are primarily attributable to an increase in net sales and an increase in write-offs coupled with an improvement in the underlying quality of our accounts receivable portfolio at December 31, 2013.

Although we believe the allowance for doubtful accounts is sufficient, a decline in economic conditions could lead to the deterioration in the financial condition of customers, resulting in an impairment of their ability to make payments and additional allowances may be required that could materially impact our consolidated results of operations. We believe our exposure to concentrations of credit risk is limited due to the large number of customers comprising our customer base and their dispersion across many different geographical regions. Additionally, we mitigate credit risk through credit insurance programs.

Inventory Valuation Reserves

Inventory valuation reserves are established in order to report inventories at the lower of weighted-average cost or market and the first-in, first-out method. As part of the valuation process, inventories are adjusted to reflect excess, slow-moving and damaged inventories at their estimated net realizable value. The valuation process for excess, slow-moving and damaged inventory contains uncertainty because management must make estimates and use judgment to determine the future salability of inventories. Inventory policies are reviewed periodically, reflecting current risks, trends and changes in industry conditions. A reserve for estimated inventory shrinkage is also maintained and reflects the results of cycle count programs and physical inventories. When preparing these estimates, management considers historical results, inventory levels and current operating trends.

Valuation of Goodwill and Indefinite Lived Intangible Assets

The recoverability of goodwill is evaluated at least annually and when events or changes in circumstances indicate that the carrying amount may not be recoverable. We have one reporting unit that is subject to goodwill impairment testing. In performing the goodwill impairment test, we use a two-step approach. The first step compares the reporting unit's fair value to its carrying value. If the carrying value exceeds the fair value, a second step is performed to measure the amount of impairment loss, if any. The identification and measurement of goodwill impairment involves the estimation of the fair value of our reporting unit and contains uncertainty because management must use judgment in determining appropriate assumptions to be used in the measurement of fair value. On January 1, 2014, we performed our annual goodwill impairment test and determined that the estimated fair value of our reporting unit significantly exceeded its carrying value.

The recoverability of indefinite lived intangibles is also evaluated on an annual basis or more often if deemed necessary. Indefinite lived intangibles not subject to amortization are assessed for impairment by comparing the fair value of the intangible asset to its carrying amount to determine if a write-down to fair value is required. Our annual impairment tests did not result in any impairment of our indefinite lived intangibles.

The estimates of fair value of our reporting unit and indefinite lived intangibles are based on the best information available as of the date of the assessment and incorporates management's assumptions about expected future cash flows and contemplates other valuation techniques. Future cash flows can be affected by changes in the industry, a declining economic environment or market conditions. There have been no events or circumstances from the date of our assessments that would have an impact on this conclusion. The carrying amount of goodwill and intangibles was \$596.5 million and \$616.8 million at December 31, 2013 and 2012, respectively. Although no impairment has been recorded to date, there can be no assurances that future impairments will not occur. An adjustment to the carrying value of goodwill and intangibles could materially impact the consolidated results of operations.

Self-Insurance Reserves

Self-insurance reserves are maintained relative to company-wide casualty insurance and health benefit programs. The level of exposure from catastrophic events is limited by the purchase of stop-loss and aggregate liability reinsurance coverage. When estimating the self-insurance liabilities and related reserves, management considers a number of factors, which include historical claims experience, demographic factors, severity factors and valuations provided by independent third-party actuaries. Management reviews its assumptions with its independent third-party actuaries to evaluate whether the self-insurance reserves are adequate. If actual claims or adverse development of loss reserves occur and exceed these estimates, additional reserves may be required. The estimation process contains uncertainty since management must use judgment to estimate the ultimate cost that will be incurred to settle reported claims and unreported claims for incidents incurred but not reported as of the balance sheet date. Reserves in the amounts of \$5.6 million and \$4.8 million at December 31, 2013 and 2012, respectively, were established related to such insurance programs.

Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial reporting basis and the tax basis of assets and liabilities at enacted tax rates expected to be in effect when such amounts are recovered or settled. The use of estimates by management is required to determine income tax expense, deferred tax assets and any related valuation allowance and deferred tax liabilities. A valuation allowance of \$0.1 million and \$0.4 million was recorded at December 31, 2013 and 2012, respectively, due to uncertainties related to the ability to utilize a portion of the deferred tax assets primarily arising from foreign net operating loss carryforwards. The valuation allowance is based on estimates of future taxable income by jurisdiction in which the deferred tax assets will be recoverable. These estimates can be affected by a number of factors, including possible tax audits or general economic conditions or competitive pressures that could affect future taxable income. Although management believes that the estimates are reasonable, the deferred tax asset and any related valuation allowance will need to be adjusted if management's estimates of future taxable income differ from actual taxable income. An adjustment to the deferred tax asset and any related valuation allowance could materially impact the consolidated results of operations.

Recent Accounting Pronouncements

Refer to Note 1 to our consolidated financial statements included in this Annual Report on Form 10-K for a discussion of new accounting pronouncements.

Results of Operations

The following table summarizes information derived from the audited consolidated statements of income expressed as a percentage of revenues for the years ended December 31, 2013, 2012 and 2011:

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Revenues	100.0%	100.0%	100.0%
Cost of sales	76.0	76.3	75.5
Gross profit	24.0	23.7	24.5
Selling, general and administrative expenses	16.8	17.2	17.8
Operating income	7.2	6.5	6.7
Interest expense, net	0.1	0.1	0.2
Income before income taxes	7.1	6.4	6.5
Income taxes	2.1	1.8	1.9
Net income	5.0	4.6	4.6
Less: net income attributable to noncontrolling interest	1.6	1.6	1.6
Net income attributable to Watsco, Inc.	3.4%	3.0%	3.0%

The following narratives include the results of operations for businesses acquired during 2012 and 2011. The results of operations for these acquisitions have been included in our consolidated statements of income beginning on their respective dates of acquisition. See Note 9 to our consolidated financial statements included in this Annual Report on Form 10-K for the pro forma financial information combining our results of operations with the operations of Carrier Enterprise II and Carrier Enterprise III. The following narratives also reflect our acquisition of an additional 10% ownership interest in Carrier Enterprise I, which became effective on July 2, 2012. We did not acquire any businesses during 2013.

In the following narratives, computations and disclosure information referring to "same-store basis" exclude the effects of locations acquired or locations opened or closed during the immediately preceding 12 months unless they are within close geographical proximity to existing locations. At December 31, 2013 and 2012, 16 and 63 locations, respectively, were excluded from "same-store basis" information. The table below summarizes the changes in our locations for 2012 and 2013:

	<u>Number of Locations</u>
December 31, 2011	542
Acquired	35
Opened	12
Closed	(16)
December 31, 2012	573
Opened	6
Closed	(10)
December 31, 2013	569

2013 Compared to 2012

Revenues

Revenues for 2013 increased \$311.6 million, or 9%, to \$3,743.3 million, including \$87.4 million attributable to the 35 new Carrier Enterprise III locations and \$2.5 million from other locations opened during the preceding 12 months, offset by \$7.9 million from locations closed. On a same-store basis, revenues increased \$229.6 million, or 7%, as compared to 2012, reflecting a 9% increase in sales of HVAC equipment (12% increase in residential HVAC equipment offset by a 2% decrease in commercial HVAC equipment), a 3% increase in sales of other HVAC products and a 3% increase in sales of commercial refrigeration products. The increase in same-store revenues is primarily due to strong demand for residential HVAC equipment.

Gross Profit

Gross profit for 2013 increased \$84.9 million, or 10%, to \$899.3 million, primarily as a result of increased revenues. Gross profit margin improved 30 basis-points to 24.0% in 2013 from 23.7% in 2012. On a same-store basis, gross profit margin also improved 30 basis-points to 24.0% in 2013 from 23.7% in 2012, primarily due to higher realized gross margins for residential HVAC equipment and non-equipment products.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for 2013 increased \$38.6 million, or 7%, to \$628.0 million, primarily as a result of increased revenues. Selling, general and administrative expenses as a percent of revenues decreased to 16.8% for 2013 from 17.2% for 2012. The decrease in selling, general, and administrative expenses as a percentage of revenues was primarily due to leveraging of fixed operating costs as compared to 2012. Selling, general and administrative expenses in 2012 included \$1.2 million of acquisition-related costs. On a same-store basis, selling, general and administrative expenses increased 3% as compared to 2012.

Operating Income

Operating income for 2013 increased \$46.3 million, or 21%, to \$271.2 million. Operating margin improved 70 basis-points to 7.2% in 2013 from 6.5% in 2012. On a same-store basis, operating income increased 19% compared to 2012.

Interest Expense, Net

Net interest expense for 2013 increased \$1.2 million, or 25%, to \$5.8 million, primarily as a result of an increase in average outstanding borrowings, partially offset by a lower effective interest rate in 2013 as compared to 2012.

Income Taxes

Income taxes increased to \$77.7 million for 2013, as compared to \$62.6 million for 2012 and are a composite of the income taxes attributable to our wholly owned operations and investments, and income taxes attributable to the Carrier joint ventures, which are taxed as partnerships for income tax purposes. The effective income tax rate attributable to us was 37.0% and 36.75% in 2013 and 2012, respectively. The increase was primarily due to higher effective tax rates for income generated by our United States subsidiaries.

Net Income Attributable to Watsco, Inc.

Net income attributable to Watsco in 2013 increased \$24.4 million, or 24%, to \$127.7 million. The increase was primarily driven by higher revenues, expanded profit margins and reduced selling, general and administrative expenses as a percent of revenues as discussed above, and by a reduction in the net income attributable to the noncontrolling interest related to Carrier Enterprise I following our purchase of an additional 10% ownership interest in Carrier Enterprise I in July 2012.

2012 Compared to 2011

Revenues

Revenues for 2012 increased \$454.0 million, or 15%, to \$3,431.7 million, including \$351.4 million attributable to the 70 new Carrier Enterprise II and Carrier Enterprise III locations and \$10.1 million from other locations opened during the preceding 12 months, offset by \$11.9 million from locations closed. On a same-store basis, revenues increased \$104.4 million, or 4%, as compared to 2011, reflecting a 5% increase in sales of HVAC equipment, a 2% decrease in sales of other HVAC products and a 21% increase in sales of commercial refrigeration products. The increase in same-store revenues is primarily due to improving demand for the replacement of residential and commercial HVAC equipment.

Gross Profit

Gross profit for 2012 increased \$86.1 million, or 12%, to \$814.4 million, primarily as a result of increased revenues. Gross profit margin declined 80 basis-points to 23.7% in 2012 from 24.5% in 2011. On a same-store basis, gross profit margin declined 90 basis-points to 23.6% in 2012 from 24.5% in 2011, due to decreased average selling prices for residential HVAC equipment and a shift in sales mix toward HVAC equipment and commercial products, which generate a lower gross profit margin than non-equipment products.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for 2012 increased \$60.2 million, or 11%, to \$589.5 million, primarily as a result of increased revenues. Selling, general and administrative expenses as a percent of revenues decreased to 17.2% for 2012 from 17.8% for 2011. The decrease in selling, general, and administrative expenses as a percentage of revenues was primarily due to leveraging of fixed operating costs as compared to 2011. Selling, general and administrative expenses in both 2012 and 2011 include \$1.2 million of acquisition-related costs. On a same-store basis, selling, general and administrative expenses were flat compared to 2011.

Operating Income

Operating income for 2012 increased \$25.9 million, or 13%, to \$224.9 million. Operating margin declined 20 basis-points to 6.5% in 2012 from 6.7% in 2011. On a same-store basis, operating income increased 1% compared to 2011.

Interest Expense, Net

Net interest expense for 2012 increased \$0.2 million, or 5%, to \$4.7 million, primarily as a result of an increase in average outstanding borrowings, partially offset by a lower effective interest rate in 2012 as compared to 2011.

Income Taxes

Income taxes increased to \$62.6 million for 2012, as compared to \$56.9 million for 2011 and are a composite of the income taxes attributable to our wholly owned operations and investments, and income taxes attributable to the Carrier joint ventures, which are taxed as partnerships for income tax purposes. The effective income tax rate attributable to us was 36.75% and 38.0% in 2012 and 2011, respectively. The decrease was primarily due to lower effective tax rates for income generated by our foreign subsidiaries and certain non-recurring tax benefits realized in 2012.

Net Income Attributable to Watsco, Inc.

Net income attributable to Watsco in 2012 increased \$12.9 million, or 14%, to \$103.3 million. The increase was primarily driven by higher revenues and reduced selling, general and administrative expenses as a percent of revenues, as discussed above, and by a reduction in the net income attributable to the noncontrolling interest related to Carrier Enterprise I following our purchase of an additional 10% ownership interest in Carrier Enterprise I in July 2012.

Liquidity and Capital Resources

We assess our liquidity in terms of our ability to generate cash to execute our business strategy and fund operating and investing activities, taking into consideration the seasonal demand of HVAC/R products, which peaks in the months of May through August. Significant factors that could affect our liquidity include the following:

- cash necessary to fund our business (primarily working capital requirements);
- the adequacy of our available bank line of credit;
- the ability to attract long-term capital with satisfactory terms;
- acquisitions;
- dividend payments;
- capital expenditures; and
- the timing and extent of common stock repurchases.

Sources and Uses of Cash

We rely on cash flows from operations and borrowing capacity under our revolving credit agreement to fund seasonal working capital needs and for other general corporate purposes, including dividend payments, if and as declared by our Board of Directors, capital expenditures, business acquisitions and development of our long-term operating strategies.

As of December 31, 2013, we had \$19.5 million of cash and cash equivalents, of which, \$12.2 million was held by foreign subsidiaries. We believe that our operating cash flows, cash on hand and funds available for borrowing under our line of credit will be sufficient to meet our liquidity needs in the foreseeable future. However, there can be no assurance that our current sources of available funds will be sufficient to meet our cash requirements.

Our access to funds under our line of credit is dependent on the ability of the syndicate banks to meet their respective funding commitments. Disruptions in the capital and credit markets could adversely affect our ability to draw on our line of credit and may also affect the determination of interest rates, particularly rates based on LIBOR, which is one of the base rates under our line of credit. Disruptions in the capital and credit markets could also result in increased borrowing costs and/or reduced borrowing capacity under our line of credit.

Working Capital

Working capital increased to \$777.6 million at December 31, 2013 from \$733.1 million at December 31, 2012, reflecting higher levels of accounts receivable and inventories commensurate with our increase in overall business volume.

Cash Flows

The following table summarizes our cash flow activity for 2013 and 2012:

	<u>2013</u>	<u>2012</u>	<u>Change</u>
Cash flows provided by operating activities	\$ 150.3	\$173.3	\$ (23.0)
Cash flows used in investing activities	\$ (14.3)	\$ (92.3)	\$ 78.0
Cash flows used in financing activities	\$ (189.0)	\$ (23.1)	\$ (165.9)

The individual items contributing to cash flow changes for the years presented are detailed in the consolidated statements of cash flows contained in this Annual Report on Form 10-K.

Operating Activities

The decrease in net cash provided by operating activities was principally attributable to changes in operating assets and liabilities, which were primarily composed of lower levels of accounts payable and other liabilities due to approximately \$18.0 million in incremental vendor payments from a one-time change in payment terms related to Carrier Enterprise II and higher accounts receivable driven by increased sales volume in 2013.

Investing Activities

The decrease in net cash used in investing activities is due to the purchase of our 60% controlling interest in Carrier Enterprise III for cash consideration of \$80.5 million in 2012, partially offset by higher capital expenditures in 2013.

Financing Activities

The increase in net cash used in financing activities was primarily attributable to net repayments under our revolving credit agreement and an increase in distributions to the noncontrolling interest in 2013, partially offset by a decrease in dividends paid in 2013 and the exercise of our option to acquire an additional 10% ownership interest in Carrier Enterprise I for \$51.9 million in 2012.

Revolving Credit Agreement

We maintain an unsecured, syndicated revolving credit agreement that provides for borrowings of up to \$500.0 million. Borrowings are used to fund seasonal working capital needs and for other general corporate purposes, including acquisitions, dividends, stock repurchases and issuances of letters of credit. Included in the facility are a \$65.0 million swingline subfacility, a \$50.0 million letter of credit subfacility and a \$75.0 million multicurrency borrowing sublimit.

On July 1, 2013, we entered into an amendment to the revolving credit agreement, which extended the maturity date from April 27, 2017 to July 1, 2018, reduced pricing, improved covenant flexibility to accommodate the seasonal nature of our working capital requirements and modified certain definitions. Borrowings under the amended credit facility bear interest at either LIBOR-based rates plus a spread, which ranges from 87.5 to 250.0 basis-points (LIBOR plus 125.0 basis-points at December 31, 2013), depending upon our ratio of total debt to EBITDA, or on rates based on the higher of the Prime rate or the Federal Funds Rate, in each case plus a spread which ranges from 0 to 150.0 basis-points (25.0 basis-points at December 31, 2013), depending upon our ratio of total debt to EBITDA. We pay a variable commitment fee on the unused portion of the commitment under the revolving credit agreement, ranging from 12.5 to 35.0 basis-points (17.5 basis-points at December 31, 2013).

At December 31, 2013 and 2012, \$230.0 million and \$316.2 million was outstanding under the revolving credit agreement, respectively. The revolving credit agreement contains customary affirmative and negative covenants, including financial covenants with respect to consolidated leverage and interest coverage ratios, and other customary restrictions. We believe we were in compliance with all covenants at December 31, 2013.

Contractual Obligations

As of December 31, 2013, our significant contractual obligations were as follows (in millions):

<u>Contractual Obligations</u>	<u>Payments due by Period</u>						<u>Total</u>
	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Thereafter</u>	
Operating leases (1)	\$65.0	\$54.5	\$43.3	\$28.3	\$14.0	\$ 8.4	\$213.5
Purchase obligations (2)	7.5	—	—	—	—	—	7.5
Total	\$72.5	\$54.5	\$43.3	\$28.3	\$14.0	\$ 8.4	\$221.0

- (1) Represents future minimum payments associated with real property, equipment, vehicles and a corporate aircraft under non-cancelable operating leases. We are committed to pay a portion of the actual operating expenses under certain of these lease agreements and these operating expenses are excluded from the table above.
- (2) Purchase obligations include amounts committed under purchase orders for goods with defined terms as to price, quantity and delivery. Purchase orders made in the ordinary course of business that are cancelable are excluded from the above table. Any amounts for which we are liable under purchase orders for goods received are reflected in Accounts Payable in our Consolidated Balance Sheets and are excluded from the above table.

Commercial obligations outstanding at December 31, 2013 under our revolving credit agreement consisted of borrowings totaling \$230.0 million with revolving maturities of 30 days.

Off-Balance Sheet Arrangements

Refer to Note 12 to our consolidated financial statements, under the caption “Off-Balance Sheet Financial Instruments,” for a discussion of standby letters of credit and performance bonds that we were contingently liable under at December 31, 2013.

Acquisitions

On July 1, 2014, we intend to exercise our option to acquire an additional 10% ownership interest in Carrier Enterprise I for approximately \$93.0 million, following which we would have an 80% controlling interest in Carrier Enterprise I.

We continually evaluate potential acquisitions and/or joint ventures and routinely hold discussions with a number of acquisition candidates. Should suitable acquisition opportunities arise that would require additional financing, we believe our financial position and earnings history provide a sufficient basis for us to either obtain additional debt financing at competitive rates and on reasonable terms or raise capital through the issuance of equity securities.

Common Stock Dividends

We paid cash dividends of \$1.15, \$7.48 and \$2.23 per share of Common and Class B common stock in 2013, 2012 and 2011, respectively. On January 2, 2014, our Board of Directors declared a regular quarterly cash dividend of \$0.40 per share of Common and Class B common stock that was paid on January 31, 2014 to shareholders of record as of January 15, 2014. Future dividends and/or dividend rate increases will be at the sole discretion of the Board of Directors and will depend upon such factors as cash flow generated by operations, profitability, financial condition, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

Company Share Repurchase Program

In September 1999, our Board of Directors authorized the repurchase, at management’s discretion, of up to 7,500,000 shares of common stock in the open market or via private transactions. Shares repurchased under the program are accounted for using the cost method and result in a reduction of shareholders’ equity. No shares were repurchased in 2013, 2012 or 2011. In aggregate, 6,370,913 shares of Common and Class B common stock have been repurchased at a cost of \$114.4 million since the inception of the program. At December 31, 2013, there were 1,129,087 shares remaining authorized for repurchase under the program.

Quantitative and Qualitative Disclosures about Market Risk

In the normal course of business we are exposed to fluctuations in foreign currency exchange rates and interest rates. To manage certain of these exposures, we use derivative financial instruments, including forward contracts and swaps. We do not use derivative financial instruments for trading purposes.

The principal foreign currency exchange rates to which we are exposed are the Canadian dollar and Mexican peso. Changes in exchange rates for these currencies may positively or negatively impact our results of operations. Revenues in these markets represent 9% and 3%, respectively, of our total revenues therefore, fluctuations in these exchange rates have not materially impacted our historical results of operations. However, as these markets grow and represent a higher percentage of our total revenues, our exposure to currency rate fluctuations could change in the future, and materially impact our results of operations.

We use foreign currency forward contracts to manage certain foreign currency transactional exposure from purchases by our Canadian operations in currencies other than their local currency. These instruments are not designated as hedging instruments. The total notional value of our foreign currency forward contracts as of December 31, 2013 was \$26.0 million, and such contracts have varying terms expiring through March 2014. See Note 12 to our consolidated financial statements, under the caption "Derivative Financial Instruments," included in this Annual Report on Form 10-K for further information.

Our revolving credit facility exposes us to interest rate risk because borrowings thereunder accrue interest at one or more variable rates. Our interest rate risk management objectives are to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve these objectives, we have historically entered into interest rate swap agreements with financial institutions that have investment grade credit ratings, thereby minimizing credit risk associated with these instruments. We do not currently hold any such swap agreements or any other derivative contracts that hedge our interest rate exposure, but we may enter into such instruments in the future.

We have evaluated our exposure to interest rates based on the amount of variable debt outstanding under our revolving credit agreement at December 31, 2013, and determined that a 100 basis-point change in interest rates would result in an impact to income before taxes of approximately \$2.3 million.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Our internal control system was designed to provide reasonable assurance to our management and Board of Directors regarding the reliability of financial reporting and the preparation and fair presentation of our published consolidated financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective may not prevent or detect misstatements and can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our Chief Executive Officer, Senior Vice President and Chief Financial Officer, we conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2013. The assessment was based on criteria established in the framework *Internal Control — Integrated Framework (1992)*, issued by the Committee of Sponsoring Organizations (“COSO”) of the Treadway Commission. Based on this assessment under the COSO framework, our management concluded that our internal control over financial reporting was effective as of December 31, 2013. The effectiveness of our internal control over financial reporting as of December 31, 2013 has been audited by KPMG LLP, an independent registered public accounting firm, as stated in their report that is included herein.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Watsco, Inc.:

We have audited Watsco, Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Watsco, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Watsco, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Watsco, Inc. and subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013, and our report dated February 27, 2014 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

February 27, 2014
Miami, Florida
Certified Public Accountants

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Watsco, Inc.:

We have audited the accompanying consolidated balance sheets of Watsco, Inc. and subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Watsco, Inc. and subsidiaries as of December 31, 2013 and 2012, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Watsco, Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 27, 2014 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

February 27, 2014
Miami, Florida
Certified Public Accountants

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

<i>(In thousands, except per share data)</i>	Years Ended December 31,		
	2013	2012	2011
Revenues	\$3,743,330	\$3,431,712	\$2,977,759
Cost of sales	2,844,077	2,617,317	2,249,465
Gross profit	899,253	814,395	728,294
Selling, general and administrative expenses	628,044	589,487	529,244
Operating income	271,209	224,908	199,050
Interest expense, net	5,830	4,665	4,458
Income before income taxes	265,379	220,243	194,592
Income taxes	77,660	62,642	56,850
Net income	187,719	157,601	137,742
Less: net income attributable to noncontrolling interest	59,996	54,267	47,292
Net income attributable to Watsco, Inc.	<u>\$ 127,723</u>	<u>\$ 103,334</u>	<u>\$ 90,450</u>
Earnings per share for Common and Class B common stock:			
Basic	<u>\$ 3.69</u>	<u>\$ 2.70</u>	<u>\$ 2.75</u>
Diluted	<u>\$ 3.68</u>	<u>\$ 2.70</u>	<u>\$ 2.74</u>

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

<i>(In thousands)</i>	Years Ended December 31,		
	2013	2012	2011
Net income	\$187,719	\$157,601	\$137,742
Other comprehensive (loss) income, net of tax			
Foreign currency translation adjustment	(16,365)	(3,191)	—
Unrealized gain on available-for-sale securities arising during the period	24	35	3
Unrealized gain on derivative instrument arising during the period	—	—	238
Other comprehensive (loss) income	(16,341)	(3,156)	241
Comprehensive income	171,378	154,445	137,983
Less: comprehensive income attributable to noncontrolling interest	53,027	52,861	47,292
Comprehensive income attributable to Watsco, Inc.	\$118,351	\$101,584	\$ 90,691

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

<i>(In thousands, except share and per share data)</i>	December 31,	
	2013	2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 19,478	\$ 73,770
Accounts receivable, net	399,565	377,655
Inventories	583,154	546,083
Other current assets	18,905	17,943
Total current assets	1,021,102	1,015,451
Property and equipment, net	45,418	42,842
Goodwill	392,610	397,262
Intangible assets, net	203,843	219,501
Other assets	6,558	6,999
	\$1,669,531	\$1,682,055
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of other long-term obligations	\$ 107	\$ 4
Accounts payable	141,104	184,957
Accrued expenses and other current liabilities	102,295	97,397
Total current liabilities	243,506	282,358
Long-term obligations:		
Borrowings under revolving credit agreement	230,044	316,182
Other long-term obligations, net of current portion	513	14
Total long-term obligations	230,557	316,196
Deferred income taxes and other liabilities	68,076	61,461
Commitments and contingencies		
Watsco, Inc. shareholders' equity:		
Common stock, \$0.50 par value, 60,000,000 shares authorized; 36,364,297 and 36,262,023 shares outstanding at December 31, 2013 and 2012, respectively	18,182	18,131
Class B common stock, \$0.50 par value, 10,000,000 shares authorized; 4,733,737 and 4,630,200 shares outstanding at December 31, 2013 and 2012, respectively	2,367	2,315
Preferred stock, \$0.50 par value, 10,000,000 shares authorized; no shares issued	—	—
Paid-in capital	606,384	592,820
Accumulated other comprehensive loss, net of tax	(11,474)	(2,102)
Retained earnings	339,362	251,475
Treasury stock, at cost, 6,322,650 shares of Common stock and 48,263 shares of Class B common stock at both December 31, 2013 and 2012	(114,425)	(114,425)
Total Watsco, Inc. shareholders' equity	840,396	748,214
Noncontrolling interest	286,996	273,826
Total shareholders' equity	1,127,392	1,022,040
	\$1,669,531	\$1,682,055

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Shares	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2010	32,449,425	\$ 19,410	\$472,883	\$ (593)	\$387,186	\$(114,425)	\$ 164,435	\$ 928,896
Net income					90,450		47,292	137,742
Other comprehensive income				241				241
Issuances of non-vested (restricted) shares of common stock	429,602	215	(215)					—
Forfeitures of non-vested (restricted) shares of common stock	(30,500)	(15)	15					—
Common stock contribution to 401(k) plan	27,240	14	1,704					1,718
Stock issuances from exercise of stock options and employee stock purchase plan	139,717	69	5,484					5,553
Retirement of common stock	(10,143)	(5)	(612)					(617)
Share-based compensation			6,340					6,340
Excess tax benefit from share-based compensation			859					859
Cash dividends declared and paid on Common and Class B common stock, \$2.23 per share					(73,276)			(73,276)
Return of capital contribution to noncontrolling interest							(32,000)	(32,000)
Fair value of noncontrolling interest							34,919	34,919
Share of carrying value of our locations contributed to joint venture							7,708	7,708
Fair value increment over carrying value of locations contributed to joint venture			7,061					7,061
Distributions to noncontrolling interest							(23,434)	(23,434)
Balance at December 31, 2011	33,005,341	19,688	493,519	(352)	404,360	(114,425)	198,920	1,001,710

Continued on next page.

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Shares	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2011	33,005,341	19,688	493,519	(352)	404,360	(114,425)	198,920	1,001,710
Net income					103,334		54,267	157,601
Other comprehensive loss				(1,750)			(1,406)	(3,156)
Issuances of non-vested (restricted) shares of common stock	111,301	56	(56)					—
Common stock contribution to 401(k) plan	26,991	13	1,759					1,772
Stock issuances from exercise of stock options and employee stock purchase plan	157,664	79	7,084					7,163
Retirement of common stock	(29,987)	(15)	(2,214)					(2,229)
Share-based compensation			7,716					7,716
Excess tax benefit from share-based compensation			1,079					1,079
Cash dividends declared and paid on Common and Class B common stock, \$7.48 per share					(256,219)			(256,219)
Common stock issued for Carrier Enterprise III	1,250,000	625	92,625					93,250
Fair value of noncontrolling interest in Carrier Enterprise III							104,244	104,244
Decrease in noncontrolling interest in Carrier Enterprise I			(8,692)				(43,189)	(51,881)
Distributions to noncontrolling interest							(39,010)	(39,010)
Balance at December 31, 2012	<u>34,521,310</u>	<u>20,446</u>	<u>592,820</u>	<u>(2,102)</u>	<u>251,475</u>	<u>(114,425)</u>	<u>273,826</u>	<u>1,022,040</u>

Continued on next page.

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Shares	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2012	34,521,310	20,446	592,820	(2,102)	251,475	(114,425)	273,826	1,022,040
Net income					127,723		59,996	187,719
Other comprehensive loss				(9,372)			(6,969)	(16,341)
Issuances of non-vested (restricted) shares of common stock	124,043	62	(62)					—
Forfeitures of non-vested (restricted) shares of common stock	(10,000)	(5)	5					—
Common stock contribution to 401(k) plan	22,551	11	1,678					1,689
Stock issuances from exercise of stock options and employee stock purchase plan	87,193	44	3,340					3,384
Retirement of common stock	(17,976)	(9)	(1,668)					(1,677)
Share-based compensation			8,760					8,760
Excess tax benefit from share-based compensation			1,511					1,511
Cash dividends declared and paid on Common and Class B common stock, \$1.15 per share					(39,836)			(39,836)
Distributions to noncontrolling interest							(39,857)	(39,857)
Balance at December 31, 2013	34,727,121	\$ 20,549	\$606,384	\$ (11,474)	\$339,362	\$(114,425)	\$ 286,996	\$1,127,392

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

<i>(In thousands)</i>	Years Ended December 31,		
	2013	2012	2011
Cash flows from operating activities:			
Net income	\$ 187,719	\$ 157,601	\$ 137,742
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	17,706	15,911	11,725
Share-based compensation	9,967	7,939	6,663
Deferred income tax provision	8,589	6,724	8,310
Provision for doubtful accounts	961	1,826	2,374
Non-cash contribution for 401(k) plan	1,689	1,772	1,718
(Gain) loss on sale of property and equipment	(156)	103	171
Excess tax benefits from share-based compensation	(1,511)	(1,079)	(859)
Changes in operating assets and liabilities, net of effects of acquisitions:			
Accounts receivable	(25,846)	(5,752)	11,987
Inventories	(40,575)	(26,652)	(22,489)
Accounts payable and other liabilities	(7,256)	11,873	(98,611)
Other, net	(1,018)	3,077	2,721
Net cash provided by operating activities	150,269	173,343	61,452
Cash flows from investing activities:			
Capital expenditures	(14,580)	(12,317)	(13,925)
Proceeds from sale of property and equipment	323	504	737
Business acquisitions, net of cash acquired	—	(80,479)	(43,455)
Net cash used in investing activities	(14,257)	(92,292)	(56,643)
Cash flows from financing activities:			
Net (repayments) proceeds under current revolving credit agreement	(83,559)	316,748	—
Distributions to noncontrolling interest	(69,494)	(16,003)	(26,469)
Dividends on Common and Class B common stock	(39,836)	(256,219)	(73,276)
Payment of fees related to revolving credit agreement	(458)	(2,116)	(38)
Purchase of additional ownership from noncontrolling interest	—	(51,881)	—
Net (repayments) proceeds under prior revolving credit agreements	—	(20,000)	10,000
Return of capital contribution to noncontrolling interest	—	—	(32,000)
Net proceeds from (repayments of) other long-term obligations	602	(1)	(69)
Excess tax benefits from share-based compensation	1,511	1,079	859
Net proceeds from issuances of common stock	2,185	5,312	5,359
Net cash used in financing activities	(189,049)	(23,081)	(115,634)
Effect of foreign exchange rate changes on cash and cash equivalents	(1,255)	127	—
Net (decrease) increase in cash and cash equivalents	(54,292)	58,097	(110,825)
Cash and cash equivalents at beginning of year	73,770	15,673	126,498
Cash and cash equivalents at end of year	\$ 19,478	\$ 73,770	\$ 15,673

Supplemental cash flow information (Note 17)

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Watsco, Inc. and its subsidiaries (collectively, "Watsco," which may be referred to as "we", "us" or "our") was incorporated in Florida in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies ("HVAC/R") in the HVAC/R distribution industry. At December 31, 2013, we operated from 569 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean.

Basis of Consolidation

The consolidated financial statements include the accounts of Watsco and all of its wholly owned subsidiaries and include the accounts of three joint ventures with Carrier Corporation ("Carrier"), in each of which Watsco maintains a controlling interest. All significant intercompany balances and transactions have been eliminated in consolidation.

Reclassifications

Certain reclassifications of prior year amounts have been made to conform to the 2013 presentation. These reclassifications had no effect on net income or earnings per share as previously reported.

Foreign Currency Translation and Transactions

Our operations in Mexico consider their functional currency to be the U.S. dollar because the majority of their transactions are denominated in U.S. dollars. Gains or losses resulting from transactions denominated in Mexican pesos are recognized in earnings within selling, general and administrative expenses in our consolidated statements of income.

The functional currency of our operations in Canada is the Canadian dollar. Foreign currency denominated assets and liabilities are translated into U.S. dollars at the exchange rates in effect at the balance sheet date, and income and expense items are translated at the average exchange rates in effect during the applicable period. The aggregate effect of foreign currency translation is recorded in accumulated other comprehensive loss in our consolidated balance sheets. Our net investment in our Canadian operations is recorded at the historical rate and the resulting foreign currency translation adjustments are included in accumulated other comprehensive loss in our consolidated balance sheets. Gains or losses resulting from transactions denominated in U.S. dollars are recognized in earnings within selling, general and administrative expenses in our consolidated statements of income.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses for the reporting period. Significant estimates include valuation reserves for accounts receivable, inventories and income taxes, reserves related to self-insurance programs and the valuation of goodwill and indefinite lived intangible assets. While we believe that these estimates are reasonable, actual results could differ from such estimates.

Cash Equivalents

All highly liquid instruments purchased with original maturities of three months or less are considered to be cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable primarily consist of trade receivables due from customers and are stated at the invoiced amount less an allowance for doubtful accounts. An allowance for doubtful accounts is maintained for estimated losses resulting from the inability of customers to make required payments. When preparing these estimates, we consider a number of factors, including the aging of a customer's account, past transactions with customers, creditworthiness of specific customers, historical trends and other information. Upon determination that an account is uncollectible, the receivable balance is written off. At December 31, 2013 and 2012, the allowance for doubtful accounts totaled \$5,737 and \$10,473, respectively.

Inventories

Inventories consist of air conditioning, heating and refrigeration equipment and related parts and supplies and are valued at the lower of cost or market using a weighted-average cost basis and the first-in, first-out methods. As part of the valuation process, inventories are adjusted to reflect excess, slow-moving and damaged inventories at their estimated net realizable value. Inventory policies are reviewed periodically, reflecting current risks, trends and changes in industry conditions. A reserve for estimated inventory shrinkage is also maintained to consider inventory shortages determined from cycle counts and physical inventories.

Vendor Rebates

We have arrangements with several vendors that provide rebates payable to us when we achieve any of a number of measures, generally related to the volume level of purchases. We account for such rebates as a reduction of inventory until we sell the product, at which time such rebates are reflected as a reduction of cost of sales in our consolidated statements of income. Throughout the year, we estimate the amount of the rebate based on our estimate of purchases to date relative to the purchase levels that mark our progress toward earning the rebates. We continually revise our estimates of earned vendor rebates based on actual purchase levels. At December 31, 2013 and 2012, we had \$9,333 and \$8,015, respectively, of rebates recorded as a reduction of inventory. Substantially all vendor rebate receivables are collected within three months immediately following the end of the year.

Marketable Securities

Investments in marketable equity securities are classified as available-for-sale and are included in other assets in our consolidated balance sheets. These equity securities are recorded at fair value using the specific identification method with unrealized holding losses, net of deferred taxes, included in accumulated other comprehensive loss within shareholders' equity. Dividend and interest income are recognized in the statements of income when earned.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization of property and equipment is computed using the straight-line method. Buildings and improvements are depreciated or amortized over estimated useful lives ranging from 3-40 years. Leasehold improvements are amortized over the shorter of the respective lease terms or estimated useful lives. Estimated useful lives for other depreciable assets range from 3-10 years.

Goodwill and Other Intangible Assets

Goodwill is recorded when the purchase price paid for an acquisition exceeds the fair value of the net identified tangible and intangible assets acquired. We evaluate goodwill for impairment annually or more frequently when an event occurs or circumstances change that indicate that the carrying value may not be recoverable. We test goodwill for impairment by first comparing the fair value of our reporting unit to its carrying value. If the fair value is determined to be less than the carrying value, a second step is performed to measure the amount of impairment loss.

Other intangible assets primarily consist of the value of trade names and trademarks, distributor agreements, customer relationships and non-compete agreements. Indefinite lived intangibles not subject to amortization are assessed for impairment at least annually, or more frequently if events or changes in circumstances indicate they may be impaired, by comparing the fair value of the intangible asset to its carrying amount to determine if a write-down to fair value is required. Finite lived intangible assets are amortized using the straight-line method over their respective estimated useful lives.

We perform our annual impairment tests each year and have determined there to be no impairment for any of the periods presented. There were no events or circumstances identified from the date of our assessment that would require an update to our annual impairment tests.

Long-Lived Assets

Long-lived assets, other than goodwill, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Recoverability is evaluated by determining whether the amortization of the balance over its remaining life can be recovered through undiscounted future operating cash flows. We measure the impairment loss based on projected discounted cash flows using a discount rate reflecting the average cost of funds and compared to the asset's carrying value. As of December 31, 2013, there were no such events or circumstances.

Fair Value Measurements

We carry various assets and liabilities at fair value in the consolidated balance sheets. Fair value is defined as the price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Fair value measurements are classified based on the following fair value hierarchy:

- Level 1 Quoted prices in active markets for identical assets or liabilities. An active market for an asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 Observable inputs other than Level 1 prices such as quoted prices in active markets for similar assets or liabilities; quoted prices in markets that are not active; or model-driven valuations or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Unobservable inputs for the asset or liability. These inputs reflect our own assumptions about the assumptions a market participant would use in pricing the asset or liability.

Revenue Recognition

Revenue primarily consists of sales of air conditioning, heating and refrigeration equipment and related parts and supplies and is recorded when shipment of products or delivery of services has occurred. Substantially all customer returns relate to products that are returned under warranty obligations underwritten by manufacturers, effectively mitigating our risk of loss for customer returns. Taxes collected from our customers and remitted to governmental authorities are presented in our consolidated statements of income on a net basis.

Advertising Costs

Advertising costs are expensed as incurred. Advertising expense for the years ended December 31, 2013, 2012 and 2011, was \$22,418, \$23,730 and \$25,052, respectively.

Shipping and Handling

Shipping and handling costs associated with inbound freight are capitalized to inventories and relieved through cost of sales as inventories are sold. Shipping and handling costs associated with the delivery of products is included in selling, general and administrative expenses. Shipping and handling costs for the years ended December 31, 2013, 2012 and 2011, was \$39,395, \$37,676 and \$30,234, respectively.

Share-Based Compensation

The fair value of stock option and non-vested (restricted) stock awards are expensed on a straight-line basis over the vesting period of the awards. Share-based compensation expense is included in selling, general and administrative expenses in our consolidated statements of income. Cash flows from the tax benefits resulting from tax deductions in excess of the compensation expense recognized for those options (windfall tax benefits) are classified as financing cash flows. Tax benefits resulting from tax deductions in excess of share-based compensation expense recognized are credited to paid-in capital in the consolidated balance sheets.

Income Taxes

We record United States federal, state and foreign income taxes currently payable, as well as deferred taxes due to temporary differences between reporting income and expenses for financial statement purposes versus tax purposes. Deferred tax assets and liabilities reflect the temporary differences between the financial statement and income tax basis of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates is recognized as income or expense in the period that includes the enactment date. We and our eligible subsidiaries file a consolidated United States federal income tax return. As income tax returns are generally not filed until well after the closing process for the December 31 financial statements is complete, the amounts recorded at December 31 reflect estimates of what the final amounts will be when the actual income tax returns are filed for that calendar year. In addition, estimates are often required with respect to, among other things, the appropriate state income tax rates to use in the various states that we and our subsidiaries are required to file, the potential utilization of operating loss carryforwards and valuation allowances required, if any, for tax assets that may not be realizable in the future.

We recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the "more-likely-than-not" threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority.

Earnings per Share

We compute earnings per share using the two-class method. The two-class method of computing earnings per share is an earnings allocation formula that determines earnings per share for common stock and any participating securities according to dividends declared (whether paid or unpaid) and participation rights in undistributed earnings. Shares of our non-vested (restricted) stock are considered participating securities because these awards contain a non-forfeitable right to dividends irrespective of whether the awards ultimately vest. Under the two-class method, earnings per common share for our Common and Class B common stock is computed by dividing the sum of distributed earnings to common shareholders and undistributed earnings allocated to common shareholders by the weighted-average number of shares of Common and Class B common stock outstanding for the period. In applying the two-class method, undistributed earnings are allocated to Common stock, Class B common stock and participating securities based on the weighted-average shares outstanding during the period.

Diluted earnings per share reflects the dilutive effect of potential common shares from stock options. The dilutive effect of outstanding stock options is computed using the treasury stock method, which assumes any proceeds that could be obtained upon the exercise of stock options, would be used to purchase common stock at the average market price for the period. The assumed proceeds include the purchase price the optionee pays, the windfall tax benefit that we receive upon assumed exercise and the unrecognized compensation expense at the end of each period.

Derivative Instruments

All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings. See Note 12, under the caption "Derivative Financial Instruments."

New Accounting Pronouncements

Reporting Amounts Reclassified Out of Accumulated Other Comprehensive Income

On January 1, 2013 we adopted guidance issued by the Financial Accounting Standards Board ("FASB") that requires disclosure for amounts reclassified out of accumulated other comprehensive income by the respective line items of net income if the amount reclassified is required to be reclassified to net income in its entirety in the reporting period. For amounts that are not required to be reclassified in their entirety to net income, a cross-reference to other disclosures that provide additional detail about those amounts is required. The adoption of this guidance did not have an impact on our consolidated financial statements.

Presentation of Unrecognized Tax Benefits

In July 2013, the FASB issued guidance that requires the presentation of an unrecognized tax benefit as a reduction to a deferred tax asset for a net operating loss carryforward rather than as a liability when the uncertain tax position would reduce the net operating loss under the tax law of the applicable jurisdiction and the entity intends to use the deferred tax asset for that purpose. This guidance is effective prospectively for interim and annual reporting periods beginning after December 15, 2013. We do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

2. EARNINGS PER SHARE

The following table presents the calculation of basic and diluted earnings per common share for our Common and Class B common stock:

<i>Years Ended December 31,</i>	2013	2012	2011
Basic Earnings per Share:			
Net income attributable to Watsco, Inc. shareholders	\$ 127,723	\$ 103,334	\$ 90,450
Less: distributed and undistributed earnings allocated to non-vested (restricted) common stock	9,064	17,656	6,045
Earnings allocated to Watsco, Inc. shareholders	<u>\$ 118,659</u>	<u>\$ 85,678</u>	<u>\$ 84,405</u>
Weighted-average common shares outstanding - Basic	<u>32,195,598</u>	<u>31,680,187</u>	<u>30,678,206</u>
Basic earnings per share for Common and Class B common stock	<u>\$ 3.69</u>	<u>\$ 2.70</u>	<u>\$ 2.75</u>
Allocation of earnings for Basic:			
Common stock	\$ 108,690	\$ 78,359	\$ 76,574
Class B common stock	<u>9,969</u>	<u>7,319</u>	<u>7,831</u>
	<u>\$ 118,659</u>	<u>\$ 85,678</u>	<u>\$ 84,405</u>
Diluted Earnings per Share:			
Net income attributable to Watsco, Inc. shareholders	\$ 127,723	\$ 103,334	\$ 90,450
Less: distributed and undistributed earnings allocated to non-vested (restricted) common stock	9,053	17,656	6,042
Earnings allocated to Watsco, Inc. shareholders	<u>\$ 118,670</u>	<u>\$ 85,678</u>	<u>\$ 84,408</u>
Weighted-average common shares outstanding - Basic	<u>32,195,598</u>	<u>31,680,187</u>	<u>30,678,206</u>
Effect of dilutive stock options	62,470	64,212	75,085
Weighted-average common shares outstanding - Diluted	<u>32,258,068</u>	<u>31,744,399</u>	<u>30,753,291</u>
Diluted earnings per share for Common and Class B common stock	<u>\$ 3.68</u>	<u>\$ 2.70</u>	<u>\$ 2.74</u>

Diluted earnings per share for our Common stock assumes the conversion of all of our Class B common stock into Common stock as of the beginning of the fiscal year, therefore, no allocation of earnings to Class B common stock is required. At December 31, 2013, 2012 and 2011, our outstanding Class B common stock was convertible into 2,704,832, 2,706,338 and 2,846,334 shares of our Common stock, respectively.

Diluted earnings per share excluded 1,066, 17,492 and 33,511 shares for the years ended December 31, 2013, 2012 and 2011, respectively, related to stock options with an exercise price per share greater than the average market value, resulting in an anti-dilutive effect on diluted earnings per share.

3. OTHER COMPREHENSIVE (LOSS) INCOME

Other comprehensive (loss) income consists of the foreign currency translation adjustment associated with our Canadian operations' use of the Canadian dollar as their functional currency, changes in the unrealized gain on available-for-sale securities and the effective portion of a cash flow hedge that matured in October 2011. The tax effects allocated to each component of other comprehensive (loss) income are as follows:

<u>Years Ended December 31,</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Foreign currency translation adjustment	<u>\$ (16,365)</u>	<u>\$ (3,191)</u>	<u>\$ —</u>
Unrealized gain on available-for-sale securities	<u>39</u>	<u>63</u>	<u>6</u>
Income tax expense	<u>(15)</u>	<u>(28)</u>	<u>(3)</u>
Unrealized gain on available-for-sale securities, net of tax	<u>24</u>	<u>35</u>	<u>3</u>
Unrealized gain on derivative instrument	<u>—</u>	<u>—</u>	<u>384</u>
Income tax expense	<u>—</u>	<u>—</u>	<u>(146)</u>
Unrealized gain on derivative instrument, net of tax	<u>—</u>	<u>—</u>	<u>238</u>
Other comprehensive (loss) income	<u>\$ (16,341)</u>	<u>\$ (3,156)</u>	<u>\$ 241</u>

The changes in accumulated other comprehensive loss, net of tax, are as follows:

<i>Years Ended December 31,</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Foreign currency translation adjustment:			
Beginning balance	\$ (1,785)	\$ —	\$ —
Current period other comprehensive loss	(9,396)	(1,785)	—
Ending balance	<u>(11,181)</u>	<u>(1,785)</u>	<u>—</u>
Available-for-sale securities:			
Beginning balance	(317)	(352)	(355)
Current period other comprehensive income	24	35	3
Ending balance	<u>(293)</u>	<u>(317)</u>	<u>(352)</u>
Derivative instrument:			
Beginning balance	—	—	(238)
Current period other comprehensive income	—	—	238
Ending balance	<u>—</u>	<u>—</u>	<u>—</u>
Accumulated other comprehensive loss, net of tax	<u>\$(11,474)</u>	<u>\$(2,102)</u>	<u>\$(352)</u>

4. SUPPLIER CONCENTRATION

We have four key suppliers of HVAC/R equipment products. Purchases from these four suppliers comprised 73%, 72% and 71% of all purchases made in 2013, 2012 and 2011, respectively. Our largest supplier, Carrier and its affiliates, accounted for 59%, 57% and 54% of all purchases made in 2013, 2012 and 2011, respectively. See Note 15. Any significant interruption by Carrier or the other key suppliers in the delivery of products could impair our ability to maintain current inventory levels or a termination of a distribution agreement could disrupt the operations of certain subsidiaries and could materially impact our consolidated results of operations and consolidated financial position.

5. PROPERTY AND EQUIPMENT

Property and equipment, net, consists of:

<i>December 31,</i>	<u>2013</u>	<u>2012</u>
Land	\$ 1,131	\$ 1,131
Buildings and improvements	49,942	48,457
Machinery, vehicles and equipment	64,012	57,130
Furniture and fixtures	20,523	18,251
	<u>135,608</u>	<u>124,969</u>
Accumulated depreciation and amortization	(90,190)	(82,127)
	<u>\$ 45,418</u>	<u>\$ 42,842</u>

Depreciation and amortization expense related to property and equipment included in selling, general and administrative expenses for the years ended December 31, 2013, 2012 and 2011, was \$11,677, \$10,986 and \$9,364, respectively.

6. DEBT

We maintain an unsecured, syndicated revolving credit agreement that provides for borrowings of up to \$500,000. Borrowings are used to fund seasonal working capital needs and for other general corporate purposes, including acquisitions, dividends, stock repurchases and issuances of letters of credit. Included in the facility are a \$65,000 swingline subfacility, a \$50,000 letter of credit subfacility and a \$75,000 multicurrency borrowing sublimit.

On July 1, 2013, we entered into an amendment to the revolving credit agreement, which extended the maturity date from April 27, 2017 to July 1, 2018, reduced pricing, improved covenant flexibility to accommodate the seasonal nature of our working capital requirements and modified certain definitions. Borrowings under the amended credit facility bear interest at either LIBOR-based rates plus a spread, which ranges from 87.5 to 250.0 basis-points (LIBOR plus 125.0 basis-points at December 31, 2013), depending upon our ratio of total debt to EBITDA, or on rates based on the higher of the Prime rate or

the Federal Funds Rate, in each case plus a spread which ranges from 0 to 150.0 basis-points (25.0 basis-points at December 31, 2013), depending upon our ratio of total debt to EBITDA. We pay a variable commitment fee on the unused portion of the commitment under the revolving credit agreement, ranging from 12.5 to 35.0 basis-points (17.5 basis-points at December 31, 2013).

At December 31, 2013 and 2012, \$230,044 and \$316,182 was outstanding under the revolving credit agreement, respectively. The revolving credit agreement contains customary affirmative and negative covenants, including financial covenants with respect to consolidated leverage and interest coverage ratios, and other customary restrictions. We believe we were in compliance with all covenants at December 31, 2013.

7. INCOME TAXES

The components of income tax expense from our wholly-owned operations and investments and our controlling interest in joint ventures with Carrier are as follows:

<i>Years Ended December 31,</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
U.S. Federal	\$62,616	\$50,919	\$50,197
State	9,234	6,245	6,338
Foreign	5,810	5,478	315
	<u>\$77,660</u>	<u>\$62,642</u>	<u>\$56,850</u>
Current	\$69,071	\$55,918	\$48,540
Deferred	8,589	6,724	8,310
	<u>\$77,660</u>	<u>\$62,642</u>	<u>\$56,850</u>

We calculate our income tax expense and our effective tax rate for 100% of income attributable to our wholly-owned operations and investments and for our controlling interest of income attributable to our joint ventures with Carrier, which are taxed as partnerships for income tax purposes.

Following is a reconciliation of the effective income tax rate:

<i>Years Ended December 31,</i>	<u>2013</u>	<u>2012</u>	<u>2011</u>
U.S. federal statutory rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit and other	3.3	2.5	3.1
Tax effects on foreign income	(1.3)	(0.8)	(0.1)
Effective income tax rate attributable to Watsco, Inc.	37.0	36.7	38.0
Taxes attributable to noncontrolling interest	(7.7)	(8.3)	(8.8)
Effective income tax rate	<u>29.3%</u>	<u>28.4%</u>	<u>29.2%</u>

The following is a summary of the significant components of our current and long-term deferred tax assets and liabilities:

<u>December 31,</u>	<u>2013</u>	<u>2012</u>
Current deferred tax assets:		
Capitalized inventory costs and inventory reserves	\$ 2,883	\$ 2,386
Self-insurance reserves	1,093	1,039
Allowance for doubtful accounts	882	1,084
Other current deferred tax assets	1,539	1,215
Total current deferred tax assets (1)	6,397	5,724
Long-term deferred tax assets:		
Share-based compensation	17,455	13,911
Other long-term deferred tax assets	909	797
Net operating loss carryforwards	283	609
	18,647	15,317
Valuation allowance	(75)	(391)
Total long-term deferred tax assets (2)	18,572	14,926
Current deferred tax liabilities:		
Other current deferred tax liabilities	(1,304)	(36)
Total current deferred tax liabilities (1)	(1,304)	(36)
Long-term deferred tax liabilities:		
Deductible goodwill	(76,519)	(66,636)
Depreciation	(2,873)	(3,100)
Other long-term deferred tax liabilities	(2,556)	(1,322)
Total long-term deferred tax liabilities (2)	(81,948)	(71,058)
Net deferred tax liabilities	<u>\$(58,283)</u>	<u>\$(50,444)</u>

(1) *Current deferred tax assets and liabilities have been included in the consolidated balance sheets in other current assets.*

(2) *Long-term deferred tax assets and liabilities have been included in the consolidated balance sheets in deferred income taxes and other liabilities.*

Amounts earned by foreign subsidiaries are generally subject to United States income taxation upon repatriation. United States income taxes have not been provided on undistributed earnings of our foreign subsidiaries. The cumulative undistributed earnings related to foreign operations were approximately \$55,000 at December 31, 2013. It is not practicable to estimate the amount of tax that might be payable. Our intention is to reinvest these earnings permanently or to repatriate the earnings only when it is tax effective to do so.

Management has determined that \$75 and \$391 of valuation allowance was necessary at December 31, 2013 and 2012, respectively, to reduce the deferred tax assets to the amount that will more likely than not be realized. At December 31, 2013, there were state and other net operating loss carryforwards of \$7,117, which expire in varying amounts from 2014 through 2026. These amounts are available to offset future taxable income. There were no federal net operating loss carryforwards at December 31, 2013.

We are subject to United States federal income tax, income tax of multiple state jurisdictions and foreign income tax. We are subject to tax audits in the various jurisdictions until the respective statutes of limitations expire. We are no longer subject to United States federal tax examinations for tax years prior to 2010. For the majority of states, we are no longer subject to tax examinations for tax years prior to 2009.

As of December 31, 2013 and 2012, the total amount of gross unrecognized tax benefits (excluding the federal benefit received from state positions) was \$3,135 and \$2,474, respectively. Of these totals, \$2,038 and \$1,609, respectively, (net of the federal benefit received from state positions) represent the amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate. Our continuing practice is to recognize penalties within selling, general and administrative expenses and interest related to income tax matters in income tax expense in the consolidated statements of income. As of December 31, 2013 and 2012, the cumulative amount of estimated accrued interest and penalties resulting from such unrecognized tax benefits was \$630 and \$583, respectively, and is included in deferred income taxes and other liabilities in the accompanying consolidated balance sheets.

The changes in gross unrecognized tax benefits are as follows:

Balance at December 31, 2010	\$1,889
Additions based on tax positions related to the current year	542
Reductions due to lapse of applicable statute of limitations	(7)
Balance at December 31, 2011	2,424
Additions based on tax positions related to the current year	416
Reductions due to lapse of applicable statute of limitations	(366)
Balance at December 31, 2012	2,474
Additions based on tax positions related to the current year	673
Reductions due to lapse of applicable statute of limitations	(12)
Balance at December 31, 2013	<u>\$3,135</u>

8. SHARE-BASED COMPENSATION AND BENEFIT PLANS

Share-Based Compensation Plan

The 2001 Incentive Compensation Plan (the "2001 Plan") provides for the award of a broad variety of share-based compensation alternatives such as non-vested (restricted) stock, non-qualified stock options, incentive stock options, performance awards, dividend equivalents, deferred stock and stock appreciation rights at no less than 100% of the market price on the date the award is granted. To date, awards under the 2001 Plan consist of non-qualified stock options and non-vested (restricted) stock. Under the 2001 Plan, we may grant awards for an aggregate of 4,000,000 shares of Common and Class B common stock. A total of 1,987,912 shares of Common stock, net of cancellations, and 1,752,642 shares of Class B common stock, net of cancellations, had been awarded under the 2001 Plan as of December 31, 2013. As of December 31, 2013, 259,446 shares of common stock were reserved for future grants under the 2001 Plan. Options under the 2001 Plan vest over two to four years of service and have contractual terms of five years. Awards of non-vested (restricted) stock, which are granted at no cost to the employee, vest upon attainment of a certain age, generally the employee's respective retirement age. Vesting may be accelerated in certain circumstances prior to the original vesting date.

The following is a summary of stock option activity under the 2001 Plan as of and for the year ended December 31, 2013:

	Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Options outstanding at December 31, 2012	324,150	\$ 56.21		
Granted	30,000	82.32		
Exercised	(79,450)	34.65		
Forfeited	(7,000)	65.31		
Expired	—	—		
Options outstanding at December 31, 2013	<u>267,700</u>	<u>\$ 65.30</u>	<u>2.65</u>	<u>\$ 8,234</u>
Options exercisable at December 31, 2013	<u>50,784</u>	<u>\$ 60.13</u>	<u>2.12</u>	<u>\$ 1,824</u>

The following is a summary of non-vested (restricted) stock activity as of and for the year ended December 31, 2013:

	Shares	Weighted-Average Grant Date Fair Value
Non-vested (restricted) stock outstanding at December 31, 2012	2,373,249	\$ 38.75
Granted	124,043	80.21
Forfeited	(10,000)	68.36
Non-vested (restricted) stock outstanding at December 31, 2013	<u>2,487,292</u>	<u>\$ 40.70</u>

The weighted-average grant date fair value of non-vested (restricted) stock granted during 2013, 2012 and 2011 was \$80.21, \$69.66 and \$63.87, respectively. The fair value of non-vested stock that vested during 2011 was \$672. No non-vested (restricted) stock vested during 2013 or 2012.

During 2011, 2,527 shares of Common stock with an aggregate fair market value of \$180 were withheld as payment in lieu of cash to satisfy tax withholding obligations in connection with the vesting of non-vested (restricted) stock.

Share-Based Compensation Fair Value Assumptions

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes option pricing valuation model based on the weighted-average assumptions noted in the table below. The fair value of each stock option award, which is subject to graded vesting, is expensed, net of estimated forfeitures, on a straight-line basis over the requisite service period for each separately vesting portion of the stock option. We use historical data to estimate stock option forfeitures. The expected term of stock option awards granted represents the period of time that stock option awards granted are expected to be outstanding and was calculated using the simplified method for plain vanilla options, which we believe provides a reasonable estimate of expected life based on our historical data. The risk-free rate for periods within the contractual life of the stock option award is based on the yield curve of a zero-coupon United States Treasury bond on the date the stock option award is granted with a maturity equal to the expected term of the stock option award. Expected volatility is based on historical volatility of our stock.

The following table presents the weighted-average assumptions used for stock options granted:

<u>Years Ended December 31,</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Expected term in years	4.25	4.25	4.25
Risk-free interest rate	0.82%	0.57%	1.12%
Expected volatility	24.56%	31.40%	32.59%
Expected dividend yield	2.20%	3.49%	3.48%
Grant date fair value	\$13.33	\$12.90	\$12.31

Exercise of Stock Options

The total intrinsic value of stock options exercised during 2013, 2012 and 2011 was \$2,753, \$5,641 and \$4,724, respectively. Cash received from Common stock issued as a result of stock options exercised during 2013, 2012 and 2011 was \$1,554, \$3,790 and \$4,530, respectively. During 2013 and 2012, 4,749 shares of Common stock with an aggregate fair market value of \$450 and 29,987 shares of Common stock with an aggregate fair market value of \$2,229, respectively, were withheld as payment in lieu of cash for stock option exercises and related tax withholdings. During 2013 and 2011, 13,227 shares of common stock with an aggregate fair market value of \$1,227 and 7,616 shares of Common stock with an aggregate fair market value of \$437, respectively, were delivered as payment in lieu of cash for stock option exercises and related tax withholdings. These shares were retired upon delivery. In connection with stock option exercises, the tax benefits realized from share-based compensation plans totaled \$1,557, \$1,245 and \$916, for the years ended December 31, 2013, 2012 and 2011, respectively.

Share-Based Compensation Expense

The following table provides information on share-based compensation expense:

<u>Years Ended December 31,</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Stock options	\$ 884	\$ 846	\$ 612
Non-vested (restricted) stock	9,083	7,093	6,051
Share-based compensation expense	<u>\$9,967</u>	<u>\$7,939</u>	<u>\$6,663</u>

At December 31, 2013, there was \$848 of unrecognized pre-tax compensation expense related to stock options granted under the 2001 Plan, which is expected to be recognized over a weighted-average period of approximately 1.6 years. The total fair value of stock options that vested during 2013, 2012 and 2011 was \$822, \$315 and \$475, respectively.

At December 31, 2013, there was \$72,870 of unrecognized pre-tax compensation expense related to non-vested (restricted) stock, which is expected to be recognized over a weighted-average period of approximately 9.7 years, of which, approximately \$53,000 is related to awards granted to our Chief Executive Officer, which vest in approximately nine years upon his attainment of age 82. In the event that vesting is accelerated for any circumstance, as defined in the related agreements, the remaining unrecognized share-based compensation expense would be immediately recognized as a charge to earnings with a corresponding tax benefit. At December 31, 2013, we were obligated to issue 177,025 shares of non-vested (restricted) stock in connection with incentive compensation agreements.

Employee Stock Purchase Plan

The Watsco, Inc. Fourth Amended and Restated 1996 Qualified Employee Stock Purchase Plan (the "ESPP") provides for up to 1,500,000 shares of Common stock to be available for purchase by our full-time employees with at least 90 days of service. The plan allows participating employees to purchase shares of Common stock with a discount of 5% of the fair market value at specified times. During 2013, 2012 and 2011, employees purchased 5,844, 6,753 and 8,520 shares of Common stock at an average price of \$79.46, \$68.76 and \$59.44 per share, respectively. Cash dividends received by the ESPP were reinvested in Common stock and resulted in the issuance of 1,899, 15,411 and 5,097 additional shares during 2013, 2012 and 2011, respectively. We received net proceeds of \$631, \$1,522 and \$829, respectively, during 2013, 2012 and 2011, for shares of our Common stock issued under the ESPP. At December 31, 2013, 525,152 shares remained available for purchase under the ESPP.

401(k) Plan

We have a profit sharing retirement plan for our employees that is qualified under Section 401(k) of the Internal Revenue Code. Annual matching contributions are made based on a percentage of eligible employee compensation deferrals. The contribution has historically been made with the issuance of Common stock to the plan on behalf of our employees. For the years ended December 31, 2013, 2012 and 2011, we issued 22,551, 26,991 and 27,240 shares of Common stock to the plan representing the Common stock discretionary matching contribution of \$1,689, \$1,772 and \$1,718, respectively.

9. ACQUISITIONS

Carrier Enterprise I

Carrier Enterprise, LLC ("Carrier Enterprise I") is a joint venture formed on July 1, 2009 with Carrier that operates a network of locations primarily throughout the Sun Belt. From its inception until July 2, 2012, we owned 60% of the joint venture and Carrier owned 40%. We had an option to purchase an additional 10% ownership interest in Carrier Enterprise I, which became exercisable on July 1, 2012. On July 2, 2012, we exercised this option and acquired an additional 10% ownership interest in Carrier Enterprise I for cash consideration of \$51,881. We have a second option to purchase an additional 10% interest in Carrier Enterprise I, which becomes exercisable beginning on July 1, 2014.

Carrier Enterprise II

On April 29, 2011, we formed a second joint venture with Carrier to distribute Carrier, Bryant and Payne branded residential, light-commercial and applied-commercial HVAC products and related parts and supplies in the northeast U.S. Carrier contributed 28 of its company-operated northeastern locations to the newly formed joint venture and we contributed 14 of our northeast locations. We purchased a 60% controlling interest in the joint venture for a fair value of \$49,229. Total consideration paid by us for our 60% controlling interest in the joint venture was composed of cash consideration of \$34,460 and our contribution of 14 northeastern locations valued at \$14,769.

The purchase price resulted in the recognition of \$32,957 in goodwill and intangibles. The fair value of the identified intangible assets was \$20,600 and consisted of \$13,400 in trade names and distribution rights and \$7,200 in customer relationships to be amortized over a 12 year period. The tax basis of the acquired goodwill recognized is deductible for income tax purposes over 15 years.

The purchase price allocation is based upon a purchase price of \$49,229, which represents the fair value of our 60% controlling interest in the joint venture. The table below presents the allocation of the total consideration to tangible and intangible assets acquired, liabilities assumed and the noncontrolling interest from the acquisition of our 60% controlling interest in the joint venture based on the respective fair values as of April 29, 2011:

Cash	\$ 5
Accounts receivable	24,300
Inventories	39,003
Other current assets	773
Property and equipment	4,402
Goodwill	12,357
Intangibles	20,600
Other assets	202
Accounts payable and accrued expenses	(22,894)
Noncontrolling interest	(29,519)
Total purchase price	<u>\$ 49,229</u>

The fair value of the noncontrolling interest was determined by applying a pro-rata value of the total invested capital adjusted for a discount for lack of control that market participants would consider when estimating the fair value of the noncontrolling interest. As a result of our contribution of 14 locations to the joint venture, \$7,708 representing 40% of the carrying value of the contributed locations was attributed to the noncontrolling interest and \$7,061 representing 40% of the difference between the fair value and carrying value of the contributed locations, was recognized as an increase to paid-in capital.

On July 29, 2011, we acquired a 60% controlling interest in Carrier's HVAC/R distribution operations in Mexico for cash consideration of \$9,000. Carrier's company-operated Mexico distribution network had revenues of approximately \$75,000 in 2010 and operated from seven locations. Products sold include Carrier's complete product line of HVAC equipment and commercial refrigeration products and supplies servicing both the residential and applied commercial markets. Collectively, the Northeast locations and the Mexico operations are referred to as "Carrier Enterprise II." Neither we nor Carrier has any options to purchase additional ownership interests in Carrier Enterprise II.

Carrier Enterprise III

On April 27, 2012, we completed the formation of a joint venture with UTC Canada Corporation ("UTC Canada"), an affiliate of Carrier, to distribute Carrier-manufactured HVAC products in Canada. The newly formed joint venture, Carrier Enterprise Canada, L.P. ("Carrier Enterprise III"), operates 35 locations throughout Canada. We have a 60% controlling interest in Carrier Enterprise III and Carrier has a 40% noncontrolling interest. Total consideration paid by us for our 60% controlling interest in Carrier Enterprise III comprised cash consideration of \$80,489 and the issuance to UTC Canada of 1,250,000 shares of Common stock, having a fair value of \$93,250. Neither we nor UTC Canada has any options to purchase additional ownership interests in Carrier Enterprise III.

The purchase price for Carrier Enterprise III resulted in the recognition of \$216,463 in goodwill and intangibles. The fair value of the identified intangible assets was \$151,172 and consisted of \$95,515 in trade names and distribution rights and \$55,657 in customer relationships to be amortized over a 15 year period. For Canadian income tax purposes, 75% of the tax basis of the acquired goodwill is amortized at a rate of 7% annually on a declining balance basis.

The purchase price allocation is based upon a purchase price of \$173,739, which represents the fair value of our 60% controlling interest in Carrier Enterprise III. The table below presents the allocation of the total consideration to tangible and intangible assets acquired, liabilities assumed and the noncontrolling interest from the acquisition of our 60% controlling interest in Carrier Enterprise III based on the respective fair values as of April 27, 2012:

Cash	\$ 10
Accounts receivable	46,718
Inventories	55,024
Other current assets	481
Property and equipment	2,517
Goodwill	65,291
Intangible assets	151,172
Other assets	978
Accounts payable and accrued expenses	(44,208)
Noncontrolling interest	(104,244)
Total purchase price	<u>\$ 173,739</u>

The fair value of the noncontrolling interest was determined by applying a pro-rata value of the total invested capital adjusted for a discount for lack of control that market participants would consider when estimating the fair value of the noncontrolling interest.

The unaudited pro forma financial information, combining our results of operations with the operations of Carrier Enterprise II and Carrier Enterprise III as if the joint ventures had been formed on January 1, 2011, is as follows:

<i>Years ended December 31,</i>	<u>2012</u>	<u>2011</u>
Revenues	\$3,526,621	\$3,404,381
Net income	156,728	159,147
Less: net income attributable to noncontrolling interest	54,153	60,380
Net income attributable to Watsco, Inc.	\$ 102,575	\$ 98,767
Diluted earnings per share for Common and Class B common stock	\$ 2.64	\$ 2.89

The foregoing unaudited pro forma financial information is presented for informational purposes only. The unaudited pro forma financial information from the beginning of the periods presented until the respective acquisition dates of the above-described Canadian, Northeast United States and Mexican operations includes adjustments to record income taxes related to our portion of Carrier Enterprise II and Carrier Enterprise III's income, amortization related to identified intangible assets with finite lives and interest expense on borrowings incurred to acquire our 60% controlling interests. This unaudited pro forma financial information does not include adjustments to add or remove certain corporate expenses of Carrier Enterprise II and Carrier Enterprise III, which may or may not be incurred in future periods, or adjustments for depreciation or synergies that may be realized subsequent to the acquisition dates. This unaudited pro forma financial information does not necessarily reflect our future results of operations or what the results of operations would have been had we acquired our 60% controlling interest in and operated Carrier Enterprise II and Carrier Enterprise III as of the beginning of the periods presented.

The results of operations of these acquired locations have been included in the consolidated financial statements from their respective dates of acquisition.

Transaction costs

Approximately \$1,200 of transaction costs is included in selling, general and administrative expenses in our consolidated statements of income for both the years ended December 31, 2012 and 2011, primarily associated with the closing and transition of Carrier Enterprise III and Carrier Enterprise II, respectively.

10. GOODWILL AND OTHER INTANGIBLE ASSETS

The changes in the carrying amount of goodwill are as follows:

Balance at December 31, 2011	\$ 319,440
Acquired goodwill	77,829
Foreign currency translation adjustment	<u>(7)</u>
Balance at December 31, 2012	397,262
Foreign currency translation adjustment	<u>(4,652)</u>
Balance at December 31, 2013	<u><u>\$ 392,610</u></u>

Other intangible assets are comprised of the following:

<u>December 31,</u>	<u>Estimated Useful Lives</u>	<u>2013</u>	<u>2012</u>
Indefinite lived intangible assets - Trade names, trademarks and distribution rights		\$138,599	\$144,683
Finite lived intangible assets:			
Customer relationships	10-15 years	80,865	84,410
Trade name	10 years	1,150	1,150
Non-compete agreements	7 years	369	369
Accumulated amortization		(17,140)	(11,111)
Finite lived intangible assets, net		<u>65,244</u>	<u>74,818</u>
		<u>\$203,843</u>	<u>\$219,501</u>

Amortization expense related to finite lived intangible assets included in selling, general and administrative expenses for the years ended December 31, 2013, 2012 and 2011, was \$6,029, \$4,925 and \$2,361, respectively. Amortization of finite lived intangible assets for 2014 through 2018 is expected to be approximately \$5,900 per year.

11. SHAREHOLDERS' EQUITY

Common Stock

Common stock and Class B common stock share equally in earnings and are identical in most other respects except (i) Common stock is entitled to one vote on most matters and each share of Class B common stock is entitled to ten votes; (ii) shareholders of Common stock are entitled to elect 25% of the Board of Directors (rounded up to the nearest whole number) and Class B shareholders are entitled to elect the balance of the Board of Directors; (iii) cash dividends may be paid on Common stock without paying a cash dividend on Class B common stock and no cash dividend may be paid on Class B common stock unless at least an equal cash dividend is paid on Common stock and (iv) Class B common stock is convertible at any time into Common stock on a one-for-one basis at the option of the shareholder.

Preferred Stock

We are authorized to issue preferred stock with such designation, rights and preferences as may be determined from time to time by our Board of Directors. Accordingly, the Board of Directors is empowered, without shareholder approval, to issue preferred stock with dividend, liquidation, conversion, voting or other rights which could adversely affect the voting power or other rights of the holders of our Common stock and Class B common stock and, in certain instances, could adversely affect the market price of this stock. We had no preferred stock outstanding at December 31, 2013 and 2012.

Stock Repurchase Plan

In September 1999, our Board of Directors authorized the repurchase, at management's discretion, of up to 7,500,000 shares of common stock in the open market or via private transactions. Shares repurchased under the program are accounted for using the cost method and result in a reduction of shareholders' equity. No shares were repurchased during 2013, 2012 or 2011. In aggregate, 6,322,650 shares of Common stock and 48,263 shares of Class B common stock have been repurchased at a cost of \$114,425 since the inception of the program. At December 31, 2013, there were 1,129,087 shares remaining authorized for repurchase under the program.

12. FINANCIAL INSTRUMENTS

Recorded Financial Instruments

Recorded financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, the current portion of long-term obligations, borrowings under our revolving credit agreement and debt instruments included in other long-term obligations. At December 31, 2013 and 2012, the fair values of cash and cash equivalents, accounts receivable, accounts payable and the current portion of long-term obligations approximated their carrying values due to the short-term nature of these instruments.

The fair values of variable rate borrowings under our revolving credit agreement and debt instruments included in long-term obligations also approximate their carrying value based upon interest rates available for similar instruments with consistent terms and remaining maturities.

Derivative Financial Instruments

We routinely use certain derivatives instruments to hedge foreign currency exposure. Although these derivatives were not designated as hedges and/or did not qualify for hedge accounting, they were effective economic hedges for the periods presented. The changes in fair value of economic hedges are recognized in earnings. During 2013 and 2012, we entered into foreign currency forward contracts to offset the earnings impact that foreign currency exchange rate fluctuations would otherwise have had on certain monetary liabilities that are denominated in nonfunctional currencies. The changes in fair value of these foreign currency forward contracts were a gain (loss) of \$315 and \$(197) for 2013 and 2012, respectively, and are included in selling, general and administrative expenses in our consolidated statements of income. The total notional value of our foreign currency exchange contracts as of December 31, 2013 was \$26,000, and such contracts have varying terms expiring through March 2014. See Note 13.

We were party to an interest rate swap agreement with a notional amount of \$10,000 that matured in October 2011 and had been designated as a cash flow hedge. The swap effectively exchanged the variable rate of 30-day LIBOR to a fixed interest rate of 5.07%. For the year ended December 31, 2011, the hedging relationship was determined to be highly effective in achieving offsetting changes in cash flows. The net change in other comprehensive loss during 2011 reflected the reclassification of \$244, net of income tax benefit of \$155, of unrealized losses from accumulated other comprehensive loss to current period earnings (recorded in interest expense, net in the consolidated statement of income).

Off-Balance Sheet Financial Instruments

At December 31, 2013 and 2012, we were contingently liable under standby letters of credit aggregating \$2,681 and \$3,098, respectively, which are primarily used as collateral to cover any contingency related to additional risk assessments pertaining to our self-insurance programs. Additionally, at December 31, 2013 and 2012, we were contingently liable under various performance bonds aggregating approximately \$800 and \$300, respectively, which are used as collateral to cover any contingencies related to our nonperformance under agreements with certain customers. We do not expect that any material losses or obligation will result from the issuance of the standby letters of credit or performance bonds because we expect to meet our obligations under our self-insurance programs and to certain customers in the ordinary course of business. Accordingly, the estimated fair value of these instruments is zero.

Concentrations of Credit Risk

Financial instruments which potentially subject us to concentrations of credit risk consist principally of accounts receivable. Concentrations of credit risk are limited due to the large number of customers comprising the customer base and their dispersion across many different geographical regions. We also have access to credit insurance programs which are used as an additional means to mitigate credit risk.

13. FAIR VALUE MEASUREMENTS

The following tables present our assets and liabilities carried at fair value that are measured on a recurring basis:

	Balance Sheet Location	Total	Fair Value Measurements at December 31, 2013 Using		
			Level 1	Level 2	Level 3
Assets:					
Available-for-sale securities	Other assets	\$265	\$ 265	—	—
Derivative financial instruments	Other current assets	\$118	—	\$ 118	—
	Balance Sheet Location	Total	Level 1	Level 2	Level 3
Assets:					
Available-for-sale securities	Other assets	\$226	\$ 226	—	—
Liabilities:					
Derivative financial instruments	Accrued expenses and other current liabilities	\$197	—	\$ 197	—

The following is a description of the valuation techniques used for these assets and liabilities, as well as the level of input used to measure fair value:

Available-for-sale securities – the investments are exchange-traded equity securities. Fair values for these investments are based on closing stock prices from active markets and are therefore classified within Level 1 of the fair value hierarchy.

Derivative financial instruments – the derivatives are foreign currency forward contracts. Fair value is based on observable market inputs, such as forward rates in active markets; therefore, we classify the derivatives within Level 2 of the valuation hierarchy.

There were no transfers in or out of Level 1 and Level 2 during 2013 or 2012.

14. COMMITMENTS AND CONTINGENCIES

Litigation, Claims and Assessments

We are involved in litigation incidental to the operation of our business. We vigorously defend all matters in which we or our subsidiaries are named defendants and, for insurable losses, maintain significant levels of insurance to protect against adverse judgments, claims or assessments that may affect us. Although the adequacy of existing insurance coverage and the outcome of any legal proceedings cannot be predicted with certainty, based on the current information available, we do not believe the ultimate liability associated with any known claims or litigation will have a material adverse effect on our financial condition or results of operations.

Self-Insurance

Self-insurance reserves are maintained relative to company-wide casualty insurance and health benefit programs. The level of exposure from catastrophic events is limited by the purchase of stop-loss and aggregate liability reinsurance coverage. When estimating the self-insurance liabilities and related reserves, management considers a number of factors, which include historical claims experience, demographic factors, severity factors and valuations provided by independent third-party actuaries. Management reviews its assumptions with its independent third-party actuaries to evaluate whether the self-insurance reserves are adequate. If actual claims or adverse development of loss reserves occur and exceed these estimates, additional reserves may be required. Reserves in the amounts of \$5,582 and \$4,844 at December 31, 2013 and 2012, respectively, were established related to such programs and are included in accrued expenses and other current liabilities in our consolidated balance sheets.

Variable Interest Entity

As of December 31, 2013, in conjunction with our casualty insurance programs, limited equity interests are held in a captive insurance entity. The programs permit us to self-insure a portion of losses, to gain access to a wide array of safety-related services, to pool insurance risks and resources in order to obtain more competitive pricing for administration and reinsurance and to limit risk of loss in any particular year. The entity meets the definition of Variable Interest Entity (“VIE”); however, we do not meet the requirements to include this entity in the consolidated financial statements. The maximum exposure to loss related to our involvement with this entity is limited to approximately \$4,400. See “Self-Insurance” above for further information on commitments associated with the insurance programs and Note 12, under the caption “Off-Balance Sheet Financial Instruments,” for further information on standby letters of credit. At December 31, 2013, there were no other entities that met the definition of a VIE.

Operating Leases

We are obligated under various non-cancelable operating lease agreements for real property, equipment, vehicles and a corporate aircraft used in our operations with varying terms through 2023. We are committed to pay a portion of the actual operating expenses under certain of these lease agreements. These operating expenses are not included in the table below. Some of these arrangements have free or escalating rent payment provisions. We recognize rent expense under such arrangements on a straight-line basis over the lease term.

At December 31, 2013, future minimum payments under non-cancelable operating leases over each of the next five years and thereafter were as follows:

2014	\$ 64,967
2015	54,508
2016	43,322
2017	28,356
2018	14,006
Thereafter	8,388
Total minimum payments	<u>\$213,547</u>

Rental expense for the years ended December 31, 2013, 2012 and 2011, was \$79,585, \$76,547 and \$70,933, respectively.

Purchase Obligations

At December 31, 2013, we were obligated under various non-cancelable purchase orders for goods aggregating approximately \$7,500, of which Carrier and its affiliates accounted for approximately \$5,600.

15. RELATED PARTY TRANSACTIONS

Purchases from Carrier and its affiliates comprised 59%, 57% and 54% of all inventory purchases made during 2013, 2012 and 2011, respectively. At December 31, 2013 and 2012, approximately \$53,000 and \$62,000, respectively, was payable to Carrier and its affiliates, net of receivables. Our joint ventures with Carrier also sell HVAC products to Carrier and its affiliates. Revenues in our consolidated statements of income for 2013, 2012 and 2011 include \$30,819, \$32,961 and \$23,710, respectively, of sales to Carrier and its affiliates. We believe these transactions are conducted at arm's-length in the ordinary course of business.

Carrier Enterprise II entered into Transactional Services Agreements ("TSAs") with Carrier, pursuant to which Carrier performed certain business processes on its behalf, including processes involving the use of certain information technologies. The services provided by Carrier pursuant to the TSAs terminated on April 30, 2012. The fees related to these TSAs were \$1,798 and \$1,139, respectively, for 2012 and 2011, and are included in selling, general and administrative expenses in our consolidated statements of income. At December 31, 2012, \$25 related to these TSAs was payable to Carrier and was included in accrued expenses and other current liabilities in our consolidated balance sheet. Amounts outstanding were repaid in 2013 and no further services are required under the TSAs for Carrier Enterprise II.

Carrier Enterprise III entered into TSAs with UTC Canada, pursuant to which UTC Canada performed certain business processes on behalf of Carrier Enterprise III, including processes involving the use of certain information technologies, and UTC Canada entered into TSAs with Carrier Enterprise III, pursuant to which Carrier Enterprise III performed certain business processes on behalf of UTC Canada. The services provided pursuant to the TSAs terminated on December 31, 2012. The fees payable by Carrier Enterprise III to UTC Canada under one TSA were substantially offset by the fees payable to Carrier Enterprise III by UTC Canada under the other TSA.

At December 31, 2012, \$29,637 was payable to Carrier and UTC Canada for unpaid distributions declared to the noncontrolling interest. This amount was paid to Carrier and UTC Canada in February 2013. No amounts were outstanding at December 31, 2013.

16. INFORMATION ABOUT GEOGRAPHIC AREAS

Our operations are primarily within the United States and Puerto Rico. Products are sold on an export-only basis to portions of Latin America and the Caribbean Basin. The following tables set forth revenues and long-lived assets by geographical area:

<i>Years Ended December 31,</i>	2013	2012	2011
Revenues:			
United States	\$ 3,325,114	\$ 3,087,256	\$ 2,938,907
Canada	318,165	240,254	—
Mexico	100,051	104,202	38,852
Total Revenues	\$ 3,743,330	\$ 3,431,712	\$ 2,977,759
<i>December 31,</i>	2013	2012	
Long-Lived Assets:			
United States	\$ 429,202	\$ 429,153	
Canada	207,340	225,076	
Mexico	5,329	5,376	
Total Long-Lived Assets	\$ 641,871	\$ 659,605	

Revenues are attributed to countries based on the location of the store from which the sale occurred. Long-lived assets consist of property and equipment, goodwill and intangible assets.

17. SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information was as follows:

<u>Years Ended December 31,</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Interest paid	\$ 5,334	\$ 2,802	\$ 1,854
Income taxes net of refunds	\$73,168	\$46,819	\$45,137
Common stock issued for Carrier Enterprise III	—	\$93,250	—
Net assets of locations contributed to Carrier Enterprise II	—	—	\$14,769

WATSCO, INC. AND SUBSIDIARIES
SELECTED QUARTERLY FINANCIAL DATA
(UNAUDITED)

(In thousands, except per share data)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Year Ended December 31, 2013					
Revenues (1)	\$713,633	\$1,120,452	\$1,081,893	\$827,352	\$3,743,330
Gross profit	175,446	266,680	258,597	198,530	899,253
Net income attributable to Watsco, Inc.	<u>\$ 13,385</u>	<u>\$ 51,318</u>	<u>\$ 45,699</u>	<u>\$ 17,321</u>	<u>\$ 127,723</u>
Earnings per share for Common and Class B common stock (2):					
Basic	<u>\$ 0.39</u>	<u>\$ 1.48</u>	<u>\$ 1.32</u>	<u>\$ 0.50</u>	<u>\$ 3.69</u>
Diluted	<u>\$ 0.39</u>	<u>\$ 1.48</u>	<u>\$ 1.32</u>	<u>\$ 0.50</u>	<u>\$ 3.68</u>
Year Ended December 31, 2012					
Revenues (1)	\$633,512	\$1,011,801	\$1,020,859	\$765,540	\$3,431,712
Gross profit	150,622	238,475	242,505	182,793	814,395
Net income attributable to Watsco, Inc.	<u>\$ 8,466</u>	<u>\$ 39,103</u>	<u>\$ 41,005</u>	<u>\$ 14,760</u>	<u>\$ 103,334</u>
Earnings per share for Common and Class B common stock (2)(3):					
Basic	<u>\$ 0.23</u>	<u>\$ 1.15</u>	<u>\$ 1.19</u>	<u>\$ 0.04</u>	<u>\$ 2.70</u>
Diluted	<u>\$ 0.23</u>	<u>\$ 1.15</u>	<u>\$ 1.19</u>	<u>\$ 0.04</u>	<u>\$ 2.70</u>

- (1) *Sales of residential central air conditioners, heating equipment and parts and supplies are seasonal. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly consistent during the year, except for dependence on housing completions and related weather and economic conditions.*
- (2) *Quarterly and year-to-date earnings per share are calculated on an individual basis; therefore, the sum of earnings per share amounts for the quarters may not equal earnings per share amounts for the year.*
- (3) *On October 31, 2012, we paid a special dividend of \$5.00 per share of Common and Class B common stock that resulted in a \$0.37 per share and \$0.33 per share reduction in diluted earnings per share for the quarter and year ended December 31, 2012, respectively.*

WATSCO, INC. AND SUBSIDIARIES
INFORMATION ON COMMON STOCK
(UNAUDITED)

Our Common stock is traded on the New York Stock Exchange (“NYSE”) and the Professional Segment of NYSE Euronext in Paris under the ticker symbol WSO. Effective February 1, 2013, the listing of our Class B common stock transferred from the NYSE MKT to the NYSE, on which it trades under the ticker symbol WSOB. The following table presents the high and low prices of our Common stock and Class B common stock, as reported by the NYSE, and, with respect to our Class B common stock for the year ended December 31, 2012, the NYSE MKT. Also presented below are dividends paid per share for each quarter during the years ended December 31, 2013 and 2012. At February 21, 2014, there were 243 Common stock registered shareholders and 96 Class B common stock registered shareholders.

	<u>Common</u>		<u>Class B Common</u>		<u>Cash Dividend</u>	
	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>Common</u>	<u>Class B</u>
Year Ended December 31, 2013:						
First quarter	\$84.25	\$74.13	\$84.38	\$74.50	\$ 0.25	\$ 0.25
Second quarter	89.16	77.72	89.48	78.19	0.25	0.25
Third quarter	95.39	85.58	96.00	85.59	0.25	0.25
Fourth quarter	<u>97.47</u>	<u>91.73</u>	<u>97.15</u>	<u>92.72</u>	<u>0.40</u>	<u>0.40</u>
Year Ended December 31, 2012:						
First quarter	\$74.97	\$66.22	\$74.00	\$67.00	\$ 0.62	\$ 0.62
Second quarter	74.60	66.39	74.00	67.50	0.62	0.62
Third quarter	79.22	66.40	79.00	66.05	0.62	0.62
Fourth quarter	<u>80.12</u>	<u>67.52</u>	<u>80.00</u>	<u>67.41</u>	<u>5.62</u>	<u>5.62</u>

SUBSIDIARIES OF THE REGISTRANT

The following table sets forth the significant subsidiaries of Watsco, Inc. as of December 31, 2013, and their respective incorporation jurisdictions. The names of various other wholly owned subsidiaries have been omitted. None of the foregoing omitted subsidiaries, considered either alone or in the aggregate as a single subsidiary, constitutes a significant subsidiary.

<u>Name of Subsidiary</u>	<u>State or Other Jurisdiction of Incorporation</u>	<u>Percent of Ownership</u>
Baker Distributing Company LLC	Delaware	100%
Carrier Enterprise Canada, L.P.	Ontario, Canada	60%
Carrier Enterprise Mexico S. de R.L. de C.V.	Mexico	60%
Carrier Enterprise, LLC	Delaware	70%
Carrier Enterprise Northeast, LLC	Delaware	60%
Carrier InterAmerica Corporation	United States Virgin Islands	70%
Carrier (Puerto Rico), Inc.	Delaware	70%
East Coast Metal Distributors LLC	Delaware	100%
Gemaire Distributors LLC	Delaware	100%
Heating & Cooling Supply LLC	California	100%

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Watsco, Inc.:

We consent to the incorporation by reference in the registration statements listed below of Watsco, Inc. of our reports dated February 27, 2014, with respect to the consolidated balance sheets of Watsco, Inc. and subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013, and the effectiveness of internal control over financial reporting as of December 31, 2013, which reports appear in the December 31, 2013 annual report on Form 10-K of Watsco, Inc.

- Form S-3 (Registration No. 333-185347)
- Form S-8 (Registration Nos. 333-185345, 333-159776, 333-149467, 333-126824, 333-86006, 333-39380, 333-82011, 333-80341, 333-10363, 33-51934, and 33-72798)

/s/ KPMG LLP

February 27, 2014
Miami, Florida
Certified Public Accountants

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Albert H. Nahmad, certify that:

1. I have reviewed this Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of this annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 27, 2014

/s/ Albert H. Nahmad

Albert H. Nahmad
Chief Executive Officer

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Barry S. Logan, certify that:

1. I have reviewed this Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of this annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 27, 2014

/s/ Barry S. Logan

Barry S. Logan
Senior Vice President

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Ana M. Menendez, certify that:

1. I have reviewed this Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of this annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 27, 2014

/s/ Ana M. Menendez

Ana M. Menendez
Chief Financial Officer

CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Watsco, Inc. ("Watsco") on Form 10-K for the year ended December 31, 2013, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Albert H. Nahmad, as Chief Executive Officer of Watsco, Barry S. Logan, as Senior Vice President of Watsco and Ana M. Menendez, as Chief Financial Officer of Watsco, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to our knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Watsco.

/s/ Albert H. Nahmad

Albert H. Nahmad
Chief Executive Officer
February 27, 2014

/s/ Barry S. Logan

Barry S. Logan
Senior Vice President
February 27, 2014

/s/ Ana M. Menendez

Ana M. Menendez
Chief Financial Officer
February 27, 2014

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Watsco and will be retained by Watsco and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by Watsco for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.